

BUSINESS CONFIDENCE INDEX

Q2 2017

11.5

Business Expectation Running Ahead of Reality



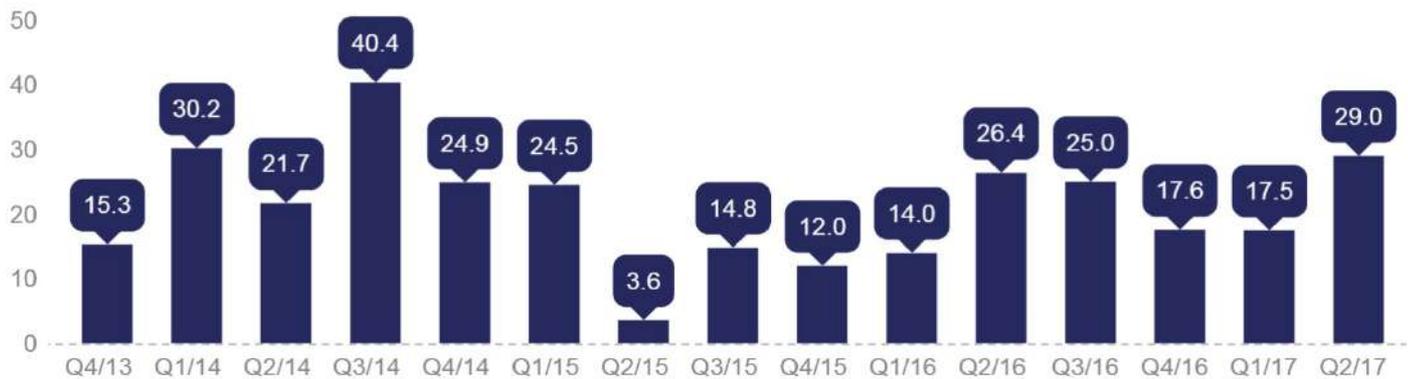
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152

SURVEY HIGHLIGHTS

Business Confidence Index (BCI)



• The Georgian Business Confidence Index (BCI)* has improved quite substantially, reaching 29.0 index points, which is an 11.5 index points improvement over the last quarter. The second quarter increase in the BCI was mostly driven by strong performance in the last quarter and quite significant improvement in expectations.

• After a significant drop of 20.8 index points in Q1, the Past Performance Index, which reflects businesses' assessment of their own economic performance in the previous quarter, posted a notable increase (up 12.3 points). Compared to other sectors, agribusinesses assessed their past performance most positively.

• The most striking result in this survey is the surge in business optimism: the Expectations Index nearly doubled, reaching 63.0 index points, which is the highest value in Georgia's BCI history! In other words, the majority of business respondents expect their performance to improve in the next quarter. Most likely such optimistic expectation is driven by the positive macroeconomic development (stabilized and even appreciated GEL) in Georgia and its' main trade and tourism partner countries. The highest increase in expectations was recorded in the manufacturing sector.

• The Sales Price Expectation Index decreased substantially. Businesses in the agricultural sector predict the highest price drop in the next quarter, as is quite normal in this time of the year.

• Large businesses demonstrated a more positive outlook compared to Small and Medium Enterprises.

• Irrespective of their size, businesses name lack of demand and finances as the main factors that limit their activities.

* The Business Confidence Index is measured on a scale of [-100; 100] points. Size of the index indicates weighted balance between the respondents giving positive and negative replies. A confidence index of 100 would indicate 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).

Overall, the BCI gained 11.5 points (on a [-100/100 scale]) compared to Q1 2017. Expectation in the private sector in Georgia were strengthened by 32.0 percentage points, and reached 63.1 index points (up from 31.1 points in Q1). Businesses' performance over the past three months significantly increased and reached nearly 22.3 points (increasing from 10.0), indicating an improvement in production/turnover/sales. Despite a huge drop in sales price expectations (from 24.3 to 7.6 index points) BCI improved, because of significant improvements in expectations and business performance.

The BCI index improved in all sectors except the construction (decreased by 10.8 points) and financial (decreased by 1.2 points) sectors. The highest increase was in the manufacturing (rising by 27.9) sector.

BCI QoQ change by sector

Sectors	Q2/17		Change
Manufacturing	46.5	▲	27.9
Construction	17.9	▼	-10.8
Retail Trade	19.7	▲	7.7
Service	28.0	▲	17.1
Agriculture	23.4	▲	0.3
Financial	49.7	▼	-1.2
Other	19.2	▲	8.1

SME



Q2/17 **Change**
17.1 ▲ **6.1**

Large



Q2/17 **Change**
31.2 ▲ **12.6**

Business confidence in the first quarter of 2017 notably improved both for large size firms and SMEs. The overall trend for large size firms is stable and positive.

It should be noted that the BCI results presented here may be overestimated, as the survey only covers businesses currently operating, and not those that have already exited the market. Firms still in operation are more likely to have a positive outlook.

Production/Turnover/Sales Past 3 Months



The actual performance of businesses significantly increased compared to the first quarter of 2017. In the Q2 2017** reporting period, sales (production or turnover) of the 211 firms surveyed increased from 10.0 (Q1 2017) to 22.3 (Q2 2017).

The current situation for firms operating in the agricultural, retail trade and service sectors significantly improved, meaning that in these sectors, weighted balance between positive and negative responses increased compared to previous quarter (for more information, see Appendix 1). However, in all other sectors, production/turnover/sales of the past three months worsened, with the highest drop in the construction sector (-30.8 percentage points).

The positive improvements in the agricultural, retail trade and service sectors overcame the slow performance of other sectors, and led to a significant overall increase in business performance.

Past 3 Months QoQ change by sector

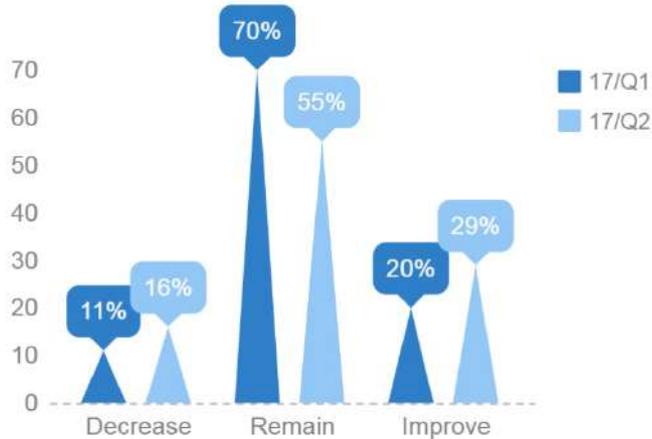
Sectors	Q2/17	Change
Manufacturing	72.2	▼ -5.8
Construction	-20.6	▼ -30.8
Retail Trade	8.0	▲ 23.3
Service	16.4	▲ 20.9
Agriculture	51.2	▲ 44.0
Financial	47.8	▼ -12.2
Other	0.0	▼ -11.9



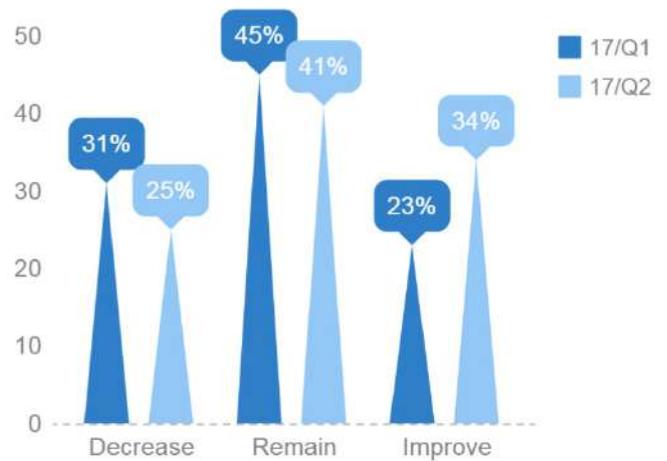
Business activities improved for both large businesses and SMEs. For large firms, business activity indicators increased from 13.2 points in Q1 2017, to 25.5 in Q2 2017; for SMEs, the same indicator increased from -2.4 to 5.1 over the same period.

** This indicator describes the activities of businesses in January, February and March

How has your firm's total employment changed over the past 3 months?



How has your business activity developed over the past 3 months?



For the majority of surveyed firms (55%), employment remained the same over the past three months, and was lower compared to the previous quarter (70%). It is also worth noting that employment over the past three months increased in 2017/Q2, from 20% to 29% of the firms surveyed.

Moreover, 41% of firms claimed that their business activities remained unchanged over the past three months, while 34% of participants stated that they had improved their performance (which was an increase of 23% over the previous quarter).

Expectations Index



The Expectations Index increased by 32.0 points in the second quarter of 2017. Expectations about the next three months strengthened in the manufacturing, service, construction, retail trade and other sectors. The highest improvement was reported in the manufacturing sector (for more information, see Appendix 1).

Aside from the drop in the agricultural and financial sectors, the other sectors are more optimistic about the future (with the highest improvement in expectations in the manufacturing sector - 60.0 percentage points).

Expectations QoQ change by sector

Sectors	17/Q2	Change
Manufacturing	60.0	▲ 60.0
Construction	75.0	▲ 17.9
Retail Trade	40.2	▲ 2.0
Service	50.0	▲ 31.0
Agriculture	61.5	▼ -24.0
Financial	27.8	▼ -26.1
Other	80.0	▲ 44.1

SME



Q2/17 **Change**
51.0 **▲ 22.9**

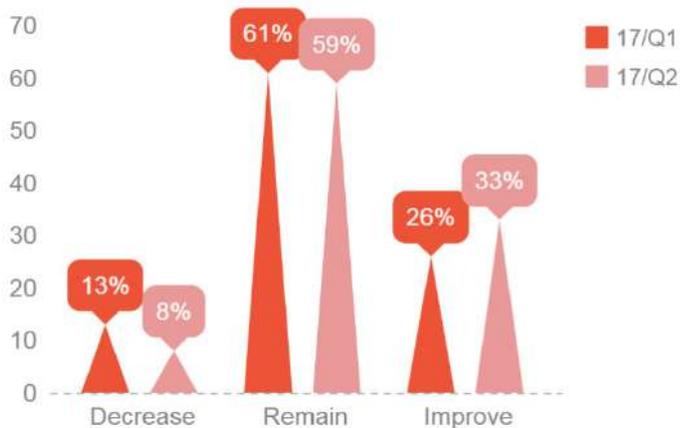
Large



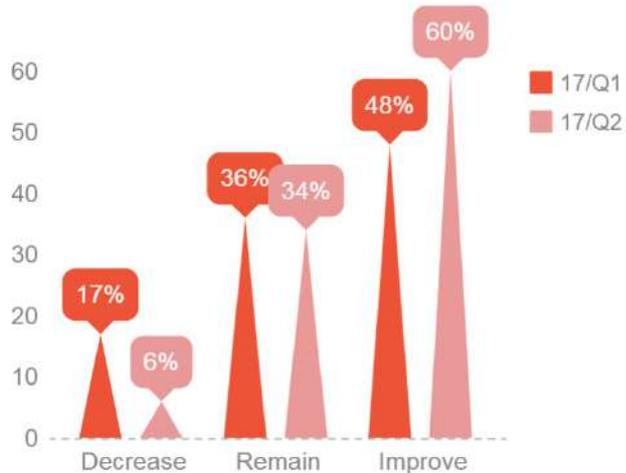
Q2/17 **Change**
65.99 **▲ 33.4**

As one can see from the table, business expectations for the three-month period April through June 2017 increased for both SMEs and large size firms. The optimism from SMEs is important, since smaller companies are more vulnerable to fluctuations in external/internal conditions.

How do you expect your firm's total employment to change over the next 3 months?



How do you expect your business condition to change over the next 3 months?



The majority (59%) of surveyed businesses did not expect any changes in employment over the next three months. Furthermore, 33% of firms stated that they would employ more employees in the future (that is higher compared to the previous quarter, by 23%).

Given the optimistic attitudes towards changes in total employment, 60% of the surveyed firms expected that the economic condition of their businesses would improve over the next three months, and 34% did not expect any changes in the future.

Sale Price Expectations



The sale price expectation index significantly decreased from 24.3 points (Q1 2017), to 7.6 points (Q2 2017).

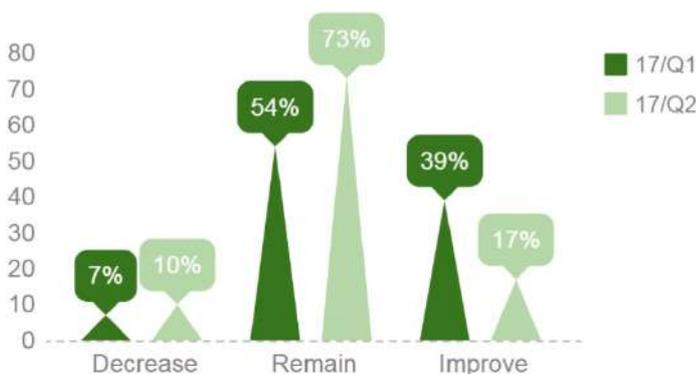
Sales prices decreased for all sectors aside from the "other" category. The agricultural sector's sales price expectations dropped and become negative, and moreover sales price expectations are the lower in this sector. The retail trade, service, construction and service sectors each expect noticeable decrease in prices in the next three months (for more information, see Appendix 1).

The overall sales price expectations index decreased for both, large companies and SMEs. However, SMEs appear to be planning a significant change (reduction) in prices for their production/services in the near future, compared to large size firms.

Sales price QoQ change by sector

Sectors	Q2/17	Change
Manufacturing	2.7	-17.5
Construction	1.0	-39.2
Retail Trade	9.9	-16.9
Service	15.6	-12.6
Agriculture	-41.6	-60.8
Other	34.4	33.1

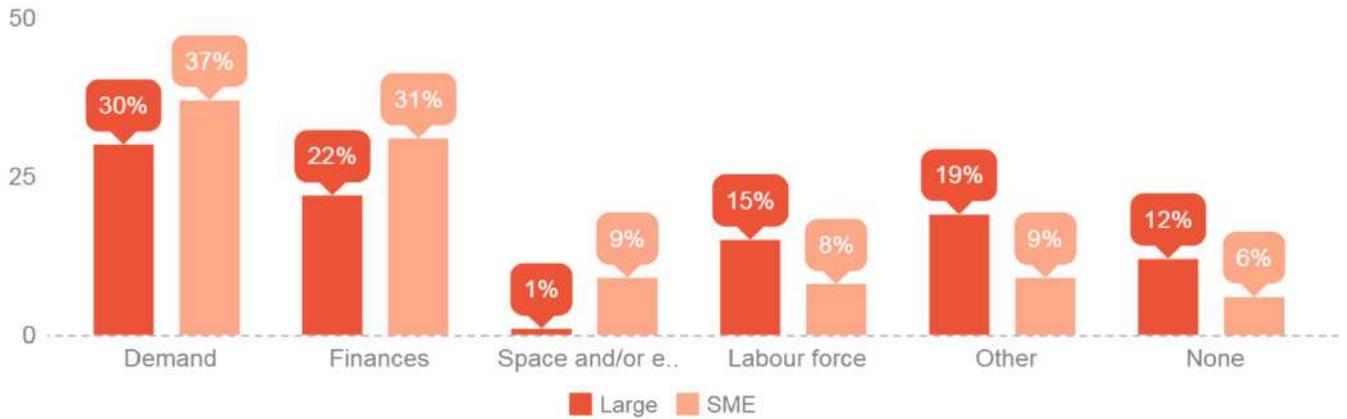
How do you expect the prices you charge to change over the next 3 months?



Q2/17	Change	Q2/17	Change
6.2	-20.1	7.9	-15.1

The majority (73%) of all surveyed firms are not going to change the prices they charge over the next three months. Only 10% of firms expect to decrease prices, and 17% expect to increase prices in the future.

WHAT ARE THE MAIN FACTORS CURRENTLY LIMITING YOUR BUSINESS? Quarter 2, 2017



Lower consumption activities and lack of access to financing are the most significant problems for businesses. One of the most limiting factors in doing business for both large firms and SMEs in Q2 2017 was lack of demand. A total of 30% of large companies and 37% of SMEs reported that lack of access to financing was their main obstacle.

According to the survey SMEs have more trouble with consumer demand than larger companies, and this pattern was evident during the second quarter.

Methodology

The ISET Policy Institute, working in partnership with the BIA (Business Information Agency) and the International Chamber of Commerce in Georgia (ICC), implemented the Business Confidence Survey beginning in 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 services 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 percentage 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.



The methodology for 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 deduced from all 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^{***} 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 for 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.

*** The size of the company is defined according to the Main Indicators' Calculation Methodology of Business Statistics (http://geostat.ge/cms/site_images/_files/georgian/methodology/business/BS_metodologia.pdf).

Distribution of Participating Firms by Sector and Size

Sectors - Number of firms	17/Q2	17/Q2	17/Q1	17/Q1
Manufacturing	8	4%	13	6%
Construction	17	8%	27	12%
Retail Trade	50	24%	50	23%
Service	97	46%	87	40%
Agriculture	15	7%	14	6%
Financial	15	7%	17	8%
Other	9	4%	10	5%
	211	% share	218	% share

Sectors	% in total turnover
Manufacturing	10%
Construction	8%
Retail Trade	17%
Service	47%
Agriculture	7%
Financial	9%
Other	3%

Sectors - Number of firms by size	17/Q2	
	Large	SME
Manufacturing	3	5
Construction	5	12
Retail Trade	9	41
Service	30	67
Agriculture	2	13
Financial	6	9
Other	4	5
	59	152

2016 Q2	
Large	SME
104	266

The number of firms participating in the BCI survey in Q2 2017 was 211. This is a decrease of nearly 3% compared to the previous quarter's level of participation. Despite the decrease in the number of participating firms, the distribution of the participating firms across sectors remained stable, and was well aligned with the distribution of firms in the economy (as depicted in Tables 1 & 2 above).

Although the distribution of the firms in our sample are well aligned with the economy, we still use turnover weights to correct for small differences between our shares (share of the number of participating firms) and economy turnover shares, even by company size.

APPENDIX 1 – BCI, Production/Turnover/Sales, Expectations, Sales Expectations by Sectors and Sizes

Overall BCI

Sales/Production/Turnover for past 3 months

Manufacturing



Manufacturing



Retail Trade



Retail Trade



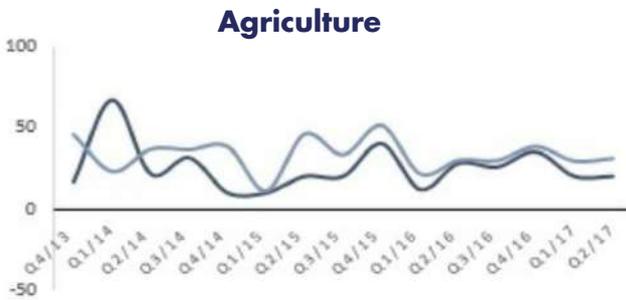
Service



Service



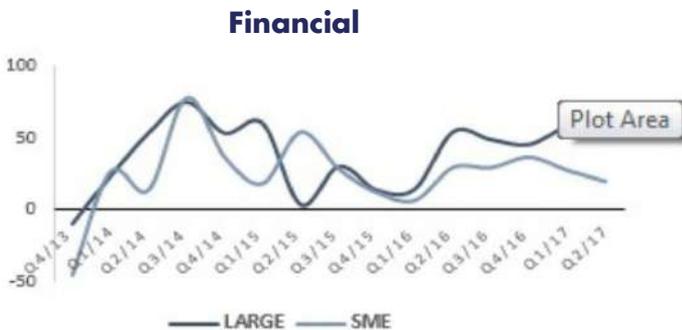
Agriculture



Agriculture



Financial

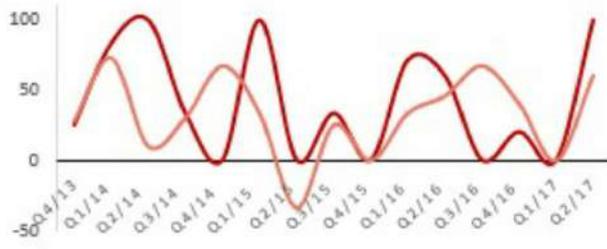


Financial

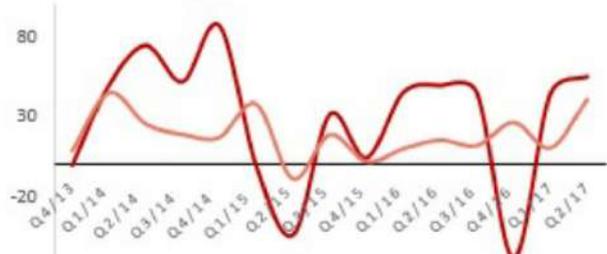


Expectations Index

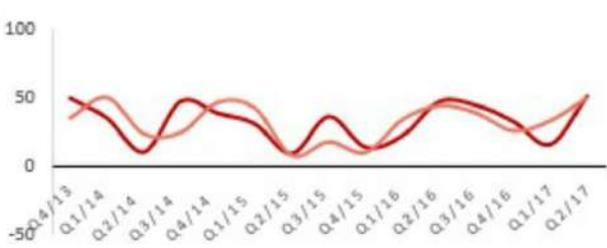
Manufacturing



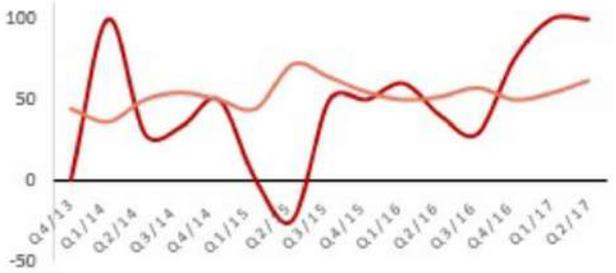
Retail Trade



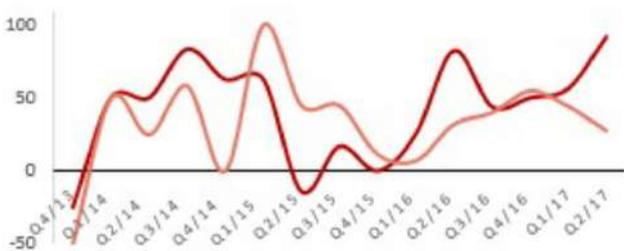
Service



Agriculture



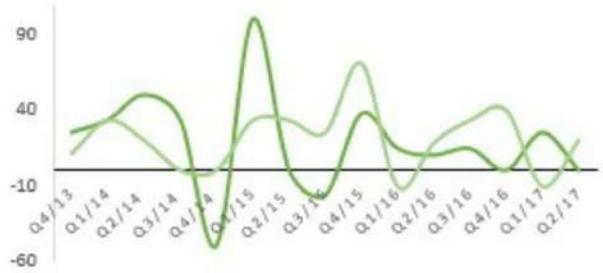
Financial



— LARGE — SME

Sales Price Expectations Index

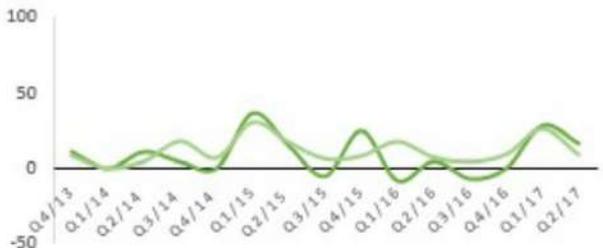
Manufacturing



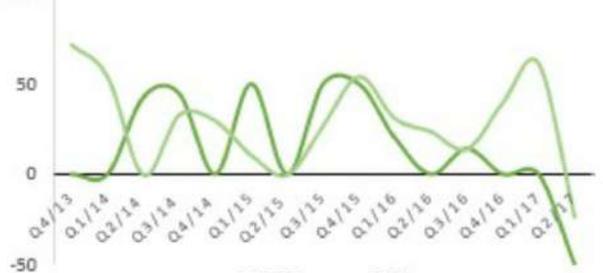
Retail Trade



Service



Agriculture



— LARGE — SME

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