

How does the increase in the transport and distribution costs, because of the global oil price changes, affect Ugandan businesses?



Photo: Fuel prices expected to destabilise the prices of goods and services
Source: RBC

Executive summary

Business Climate Index (BCI) improved by twenty-eight index points to 86.22 but remained below the full potential. The immense improvement is attributed to the onset of the Christmas season coupled with business-related factors such as improved demand for goods, access to regional markets and international markets, and improvements in internal business operations. The improvement was primarily driven by the advancement in the business perceptions in the manufacturing sector. The favourable sentiments in the manufacturing sector are attributed to the improvement in the business environment, increased profits, availability of skilled labour force, better product prices and reduced input costs. Nonetheless, the positive sentiments in the manufacturing sector were negated by the deterioration in some indices both in the agriculture and services sectors. The agricultural sector drop emanated from the onset of adjustment in transport fares resulting from the rise in international oil prices, making transportation of agricultural inputs and output challenging. While the restrictive and mandatory COVID-19 testing and follow up of cases for all incoming travelers at the five major points of entry could explain the service sector's poor performance relative to manufacturing and agriculture. Business perceptions and expectations for the next quarter (January-March 2022) remain optimistic on account of anticipation by businesses regarding reduction in input costs, ability to expand/start new businesses, favourable business environment and activity.

Data and methods

The data used in computing the Business Climate Index (BCI) is a panel of businesses based on the Uganda Bureau of Statistics Census of Business Establishment 2011, first tracked in 2012. This current quarterly bulletin covered 170 business establishments. Overtime, panel element has enabled us to track the business environment in Uganda. is computed based on the following business evaluation indicators: business activity, turnover, profitability, incoming new business, capacity utilisation, average costs of inputs, price of produced

goods, business optimism, number of employees, and monthly average wage. For each of the evaluation indicators, respondents are asked to express their perceptions on a Likert scale as follows: "improved", "did not change", "declined" or "above normal for the quarter", "normal for the quarter", "below average for the quarter" or "more favourable", "unchanged", "less favourable". These responses are coded as 0, 1, and 2, respectively. In this case, if a respondent's perception of the business environment is that it deteriorated, such a response would be coded 0, it would be coded one if the business climate did not change, and 2 if the business climate improved.

The index does not consider the magnitude of change in the data but considers the general direction of movement in the key indicators. The index is sensitive to the direction instead of the magnitude of the change in business conditions. During the data collection process, we ask business managers to assess the general economic environment for the current quarter relative to the previous quarter; and their expectations for the next quarter. Based on the business evaluation indicators explained earlier, the business climate index is computed as the weighted arithmetic means of indices of the individual business evaluation indicators. The indices range from 0 – 200. The interpretation of the BCI is such that it scores above 100, point to an improving business climate. Scores below 100, imply that the general business conditions are getting worse. And a score of 100, points to unchanged business conditions.

Also, the index analyses the evolution of challenges facing businesses during October-December 2021 by identifying which business constraints became more of a problem and less of a problem. We also ask business managers to indicate how each identified business constraint has evolved during the quarter. For each of the business constraints, we asked if it was “more of a problem”, “unchanged”, or “less of a problem”. The resultant weighted indices range from -100 to 100, with positive scores suggesting that a particular constraint is perceived to be more of a problem in the current quarter; negative scores imply that a constraint is less of a problem, and zero scores point to business constraint whose severity has remained unchanged.

Results

Business climate improves, future expectations optimistic

Results indicate that the Business Climate Index improved immensely though below potential by 28 percentage points to 86.2 during the current quarter (October-December, 2021), from 58.3 in the previous quarter (July-September, 2021). The improvement was against the backdrop of improvement in the general business environment, capacity utilisation, better product prices and favourable labour costs. Figure 1 shows that the conditions for doing business as captured by the BCI index improved immensely.

The improvement was driven by the onset of the Christmas season (Figure 1). In particular, the easing of the COVID-19 containment measures such as the Standard Operating Procedures (SOPs), especially in public transportation, enhances the movement of people, goods, and services from one place to another. Indeed, the 2021 Christmas season is the first festive period in two years to be celebrated without COVID-19 restrictions.¹ In addition, the improvement in business perceptions was driven by the improvement in demand, internal business processes, and

regional and international markets. Conversely, the current index (86.2 percent) remains below potential due to high input costs, low business optimism, low product prices, and low business activity. Furthermore, business managers reported corruption and bribery, insufficient demand, unfavourable macroeconomic factors, and unfavourable tax policy as persistent binding constraints to the business environment.

Nonetheless, figure 1 indicates that businesses managers interviewed expect an improvement in the business environment in the coming quarter (January-March 2022). This sentiment is primarily driven by an anticipated decline in input costs, ability to start/expand businesses, capacity utilisation, availability of skilled labour force, favourable business environment and activity.

The business climate index by sector

During the current quarter, the conditions for doing business improved across the entire economic spectrum; agriculture, manufacturing and service sector though, the marginal change in the agriculture sector was smaller relative to the manufacturing and service sector. The respective index for the agriculture, manufacturing and services sector improved to 97.2, 120 and 82 points, compared to 88, 74.2 and 55.4 points in the previous quarter, respectively (Figure 2). The conditions for doing business in the manufacturing sector hit a record 100 points mark for the first time since the third quarter of 2019.

The positive sentiments in the manufacturing sector were favoured by; improvement in the general business environment, better product prices, optimum capacity utilisation, and availability of labour. In addition, perceptions of business conditions in the agriculture sector registered the second-best improvement. However, the changes were relatively minimal- a rise of 10.51 points to 97.2 from 87.7 from the previous quarter. Improvement in the agriculture sector was against a backdrop of lower input costs, resulting in better prices, increased business turnover, increased profits, and expansion of businesses. The minimal improvement in the agricultural could be attributed to the COVID-19 stimulus packages to small businesses to enhance business recovery and economic growth during the current quarter.

In the service sector, business sentiments increased by 26.6 points to 81.9 in the current quarter from 55.4 in the previous quarter. The improvement in the service sector was driven by increased labour availability, increased sales turnover, increased profitability, and a favourable business environment. However, the strict COVID-19 restrictions in the current quarter, such as the mandatory COVID-19 testing and follow up of cases for all incoming travellers at the five major points of entry, could explain the service sector's poor performance relative to the manufacturing and agriculture sectors.²

1 <https://www.monitor.co.ug/uganda/business/prosper/counting-the-real-cost-of-christmas-3665528>

2 <https://www.monitor.co.ug/uganda/news/national/omicron-uganda-sets-tougher-rules-for-travellers-3657410>

Figure 1 The Business Climate Assessment

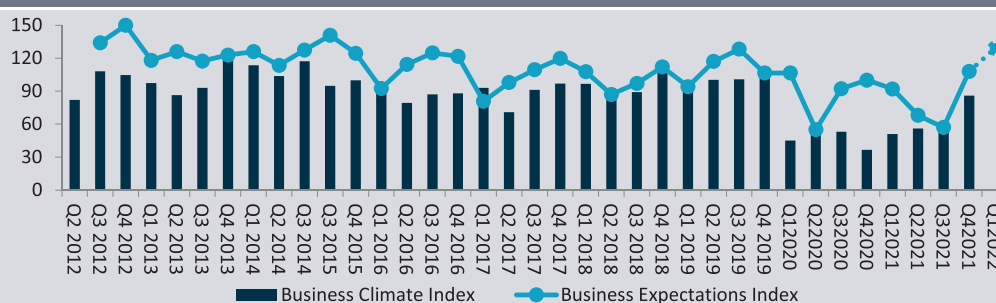
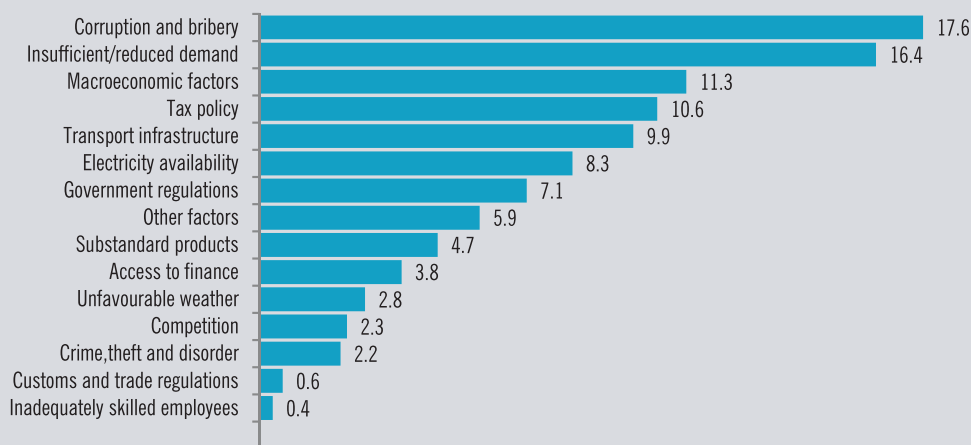


Figure 2 Business Climate Index by Sector**Figure 3 Business Constraints (%)**

Challenges in doing business

Unlike the previous quarter (April-June, 2021), the top five most important constraints in doing business for the current quarter comprised corruption, bribery, and insufficient demand. This was besides the persistent business challenges (macroeconomic factors, tax policy, transport infrastructure, and electricity unavailability) that have not changed since the last quarter. This suggests that major policy and regulatory constraints facing Ugandan businesses are persistent. The corruption and bribery issues raised in the current quarter is partly attributed to the suspension of Visas issuance at Entebbe International Airport following the outbreak of COVID-19 in 2020. This has exposed the majority of Ugandans, especially business people to forced bribes for Visas in order to make trips in and out of the country³. Indeed, despite the numerous legal provisions and systems aimed at fighting corruption, the government still struggles to end the vice. According to the latest 2021 Corruption Perception Index (CPI) released by Transparency International (TI), Uganda has slipped three places to 144th position in the global ranking out of the 180 rated countries, with a score of 27%, which also indicates a backslide from 28% in 2019⁴. While in the East African region, Uganda ranks fourth with a 27%, behind Rwanda (53%), Tanzania (39%), and Kenya (30%).

Regarding insufficient demand, the Bank of Uganda attributes insufficient demand to a decline in real income, “Since inflation has averaged at 2.2 percent while economic growth has been subdued, majority of households could be facing real income decline rather than a

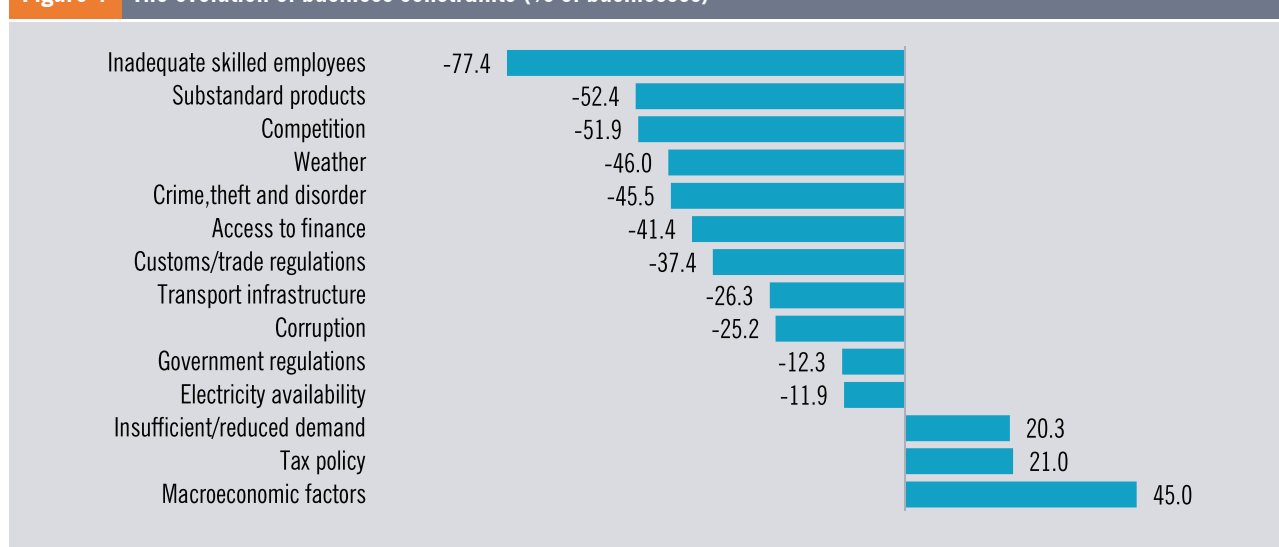
rise in the cost of living rising”.⁵ Furthermore, the World Bank indicates that real incomes dropped resulting from COVID-19 containing measures and increased uncertainty in the conditions of doing business. This has reduced growth in employment private consumption, thereby leading to a slowdown in economic growth.

Unlike in the previous quarter, where government regulation, insufficient/reduced demand and tax policy became more of a problem. Figure 4 shows that in the current quarter, macroeconomic factors, insufficient demand and tax policy were perceived to have elevated. A decline in real incomes resulting from COVID-19 containing measures and increased uncertainty in the conditions of doing business could explain why reduced demand is perceived as a problem. In addition, tax policy was also reported to be more of a problem in the current quarter as in the previous, because of a severe decline in the capacity of businesses to meet their tax obligations due to the subdued demand and sales turnover. Similar to the previous quarter, inadequately skilled employees, substandard products, weather and competition became less of a problem in the period under review.

³ <https://www.monitor.co.ug/uganda/special-reports/ugandans-query-e-visa-system-amid-delays-claims-of-bribery-3633986>

⁴ <https://www.newvision.co.ug/articledetails/125783>

⁵ <https://www.monitor.co.ug/uganda/business/prosper/is-it-inflation-or-reduction-in-incomes-3636932>

Figure 4 The evolution of business constraints (% of businesses)**Future business outlook: October-December 2021**

Unlike the previous quarter, businesses are optimistic about the near term developments. The expected index for January-March 2022 is 129, as indicated in Figure 1, which is 21.41 points higher than the current quarter's expectation which is 86.2 points. Generally, further improvement in the business condition is expected to take shape mostly from anticipated general improved business activity, capacity utilisation, reduced input costs, production costs, ability to expand/start up new businesses and high business optimism heightened by the anticipated lifting of curfew and total re-opening of the economy from the COVID-19 lockdown.

Furthermore, sectoral breakdown indicates that sector differences are expected to exist in the business environment. In this regard, lower business confidence is expected in the agriculture sector relative to the manufacturing and service sectors. In particular, the agriculture sector is expected to suffer more than the two sectors (service and manufacturing). The expected indices are 101, 143, and 130 for agriculture, manufacturing, and services. The anticipated improvement in business conditions in the manufacturing sector is attributable to the anticipated improvement in inputs availability, business environment, capacity utilisation, new businesses, and positive optimism.

On the contrary, the expected unfavourable business environment in the agriculture sector is anchored around the anticipated decline of product prices, profits, inability to expand/start a new business, high input costs, unfavourable business activity and low business turnover resulting from the decline in the real income.

The business climate is expected to be at 129.2, and this is 21.2 percentage points above the current quarter's expectation. The expected improvement in the overall business climate is projected to be driven by the anticipated rise in demand, improvement in international markets, internal business improvements and regional dynamics. In addition, all indices are expected to improve to the above full potential. The expected improvement is also attributed to the lifting of curfew restriction and re-opening of the night economy.

The sectoral breakdown indicates expected rise in the expected business confidence for the agriculture sector from the current 84 to 101, and improvement in both the manufacturing and services sector from 122 and 107 to 143 and 130 respectively for the next quarter. The expected rise in agriculture sector index is due to expected improvement on some

indices i.e., favourable environment, business optimism, capacity utilisation, favourable business activity and a rise in business turnover.

Question of the quarter

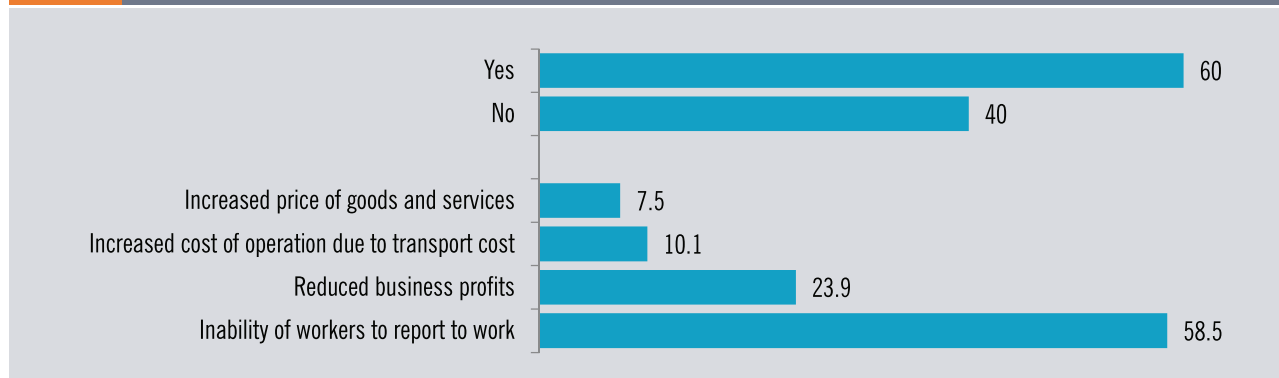
In this quarter, we sought to understand the effect of adjusted transport fares on the performance of businesses. The United Bus Owners Association (UBOA) suggest that the new fares are based on a consultative meeting following the increase of fuel prices in the months of October and November to enable the transporters continue serving their customers.⁶ In particular, we asked: a) "Has your business been affected by the adjustment in the transport fares?" b) "If yes, how has your business been affected?"

Results (Figure 5) indicate that 60 percent of the businesses were affected by the newly adjusted transport fare. The remaining 40 percent were not affected by the new transport fares. The new adjustment in transport fare has consequential impact to the degree of movement of goods, services and factors of production from one place to another.

Among those who were affected by the adjusted transport fares, about 59 percent reported that the new adjusted transport fare reduces the ability of workers to report to work and 24 percent reported that adjusted transport fares reduce business profits. The results reveal the need for government to subsidise fuel prices in order to mitigate the high fuel prices and make transport costs cheaper to business owners. The government could also enforce distribution and margin costs regulatory measures as a way of limiting fuel profit, margin-fuel control regime.

⁶ <https://www.monitor.co.ug/uganda/news/national/bus-operators-explain-hike-of-transport-fares--3638996>

Figure 5 Effect of the adjusted transport fare on business performance, %



Conclusion

Sentiments about doing business in Uganda in the current quarter (October-December 2021) immensely improved relative to the previous quarter (July-September 2021). Despite the immense improvement in the conditions for doing business, the index is still below potential (100) points. Nonetheless, some sub-indices, namely business environment, capacity utilisation, better product prices and better salaries were all above potential (100), reflecting the Christmas seasons euphoria.⁷

Similar with the previous quarter, some business constraints persisted. In this regard, corruption and bribery, insufficient demand, macroeconomic factors, tax policy, poor transport infrastructure, electricity unavailability and increased government regulation in the current quarter (October-December, 2021). Considering future expectations, business perceptions for the next quarter (January-March, 2021) is more optimistic across all sectors. The next quarter will see above potential for all sectors; agriculture, manufacturing and services.

The BCI for the current quarter improved to 86.2 index points. Despite remaining below potential, some indices such as business environment, capacity utilisation product cost and salary were above full potential (100) owing to the onset of the Christmas season. In addition, sector breakdown shows improvement in index across the three sectors under

consideration; agriculture, manufacturing sector, and services.

The below full potential index for the current quarter is due to the persistence of some challenges to doing business such as low business activity, low sales turnover, low profits, inability to expand/start new business, low business optimism and inadequate skilled labour force.

The projection for the next quarter (January -March 2022) indicates expected improvement from the current 108 to 129.2. This is majorly due to the expected decline in input cost, favourable business environment, improvement in business activity, ability to expand/start business and available skilled labourforce due to the anticipated lifting of the lockdown restriction such as curfew hours and full re-opening of the economy. In addition, sector breakdown indicates expected improvement in BCI across all three the sectors; agriculture, manufacturing and services sector, to 100.2, 143.1 and 129.6 respectively.

Considering the effect of the adjusted transport fare on the operation of businesses, most of the businesses are faced a challenge of worker absenteeism due to inability to report to work, while faced reduced business profits. Worst of all some faced increased cost of produced and thus could not sustain their stay in business.

⁷ <https://www.monitor.co.ug/uganda/business/prosper/counting-the-real-cost-of-christmas-3665528>

The Economic Policy Research Centre (EPRC) has been producing the Business Climate Index (BCI) for Uganda since June 2012. The BCI reflects the perceptions of Ugandan business managers on the current and near-future (expected three months ahead) business conditions. The BCI is a perceptions indicator of economic activity and the general business environment in which businesses operate. The purpose of BCI is to forecast turning points in economic activity and thus provide critical information for policy makers both in Government and the Private Sector.

About EPRC

The Economic Policy Research Centre (EPRC) is an autonomous not-for-profit organization established in 1993 with a mission to foster sustainable growth and development in Uganda through advancement of research – based knowledge and policy analysis.

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