ECONOMIC POLICY RESEARCH CENTRE

Towards Sustainable Development

The Uganda Business Climate Index

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Partial easing of the COVID-19 lockdown improves the business climate, but it remains below potential.

Business bussing in downtown Kikuubo market area, Kampala after the announcement of partial easing of the COVID-19 lockdown.

Source: https://www.newvision.co.ug/news/1521307/downtown-kampala-pictures, 22nd June 2020

Executive Summary

The Business Climate Index (BCI) slightly improved by about 11.6 basis points from 45.2 in the previous quarter (January-March 2020) to 56.8 in the current quarter (April-June 2020). The slight improvement was driven by a rise in business perceptions across all sectors. The favourable perceptions across all the three sectors are attributed to the partial opening of the selected sectors of the economy from the COVID-19 pandemic lockdown during the current quarter. In terms of business constraints, insufficient demand, limited access to finance and concerns over the cost and reliability of electricity supply continue to constrain business competitiveness, and their severity was perceived to have been elevated during the current period. Perceptions about business sentiment in the next quarter (July – September 2020) are favourable on account of the expected recovery in domestic demand, product prices, capacity utilisation and incoming new business, possibly signalling business recovery after the effects of the COVID-19 pandemic lockdown.

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 166 business establishments. The panel element has enabled us to track the business environment in Uganda over time.

The BCI is computed based on the following business evaluation indicators: level of business activity, turnover, profitability, incoming new business, capacity utilisation, average costs of inputs, price of produced goods, business optimism, number of employees, and average monthly salary. 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 1 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. As such, the index is sensitive to the direction as opposed to 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 a similar period a year earlier; 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 mean of indices of the individual business evaluation indicators. The indices range from 0 – 200. The interpretation of the BCI is such that 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 April-June 2020 by identifying which business constraints are more of a problem and less of a problem. We also ask business managers to indicate how each of the identified business constraints has evolved over the last full year. 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

Restricted partial opening up of the economy improves business climate, and future perceptions are upbeat.

Results indicate a slight improvement in the conditions for doing business in the current quarter (April – June 2020), having improved from a generally pessimistic trend over the previous quarter (Figure 1). During the current quarter, the perceptions for doing business improved by 11.6 basis points to 56.8 during the current quarter (April-June 2020), from 45.2 in the preceding quarter (January-March 2020). Despite this increase, the overall perceptions remained below potential. The rise in the index is an indicator of improving conditions for doing business in Uganda during the period under review. In particular, the sub-indices for labour cost (68.4), business turnover (48.2), business activity (46.5) and prospects for the establishment of new businesses (53.7), all registered significant improvement compared to the previous quarter.

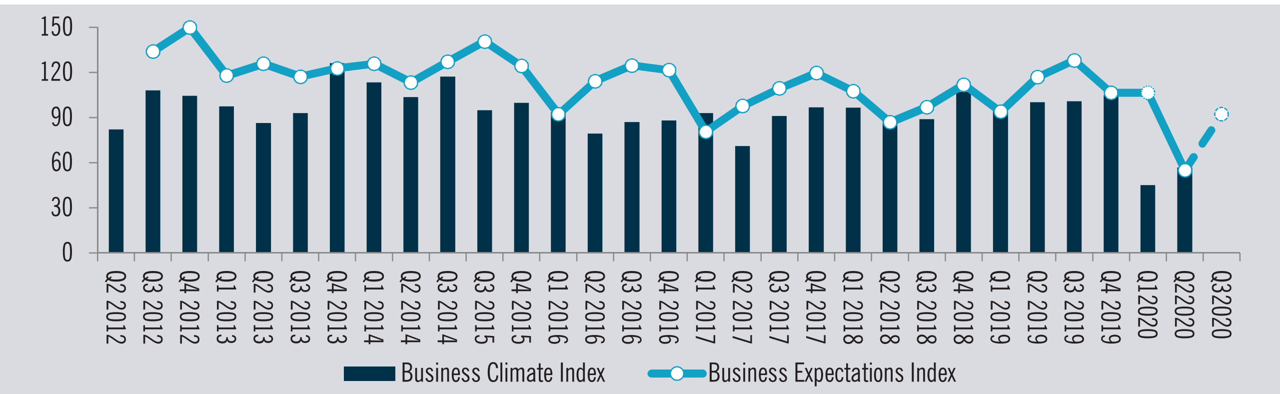
The positive sentiment in the business environment in the current quarter was driven mainly by the partial easing of the COVID-19 containment measures that had been previously instituted for 43 days to fight the spread of the coronavirus. Notably, during the quarter, Government announced a restricted opening of the following sectors namely; agriculture, insurance, professional services, education, construction, hardware shops, wood and metal workshops, vehicle garages, restaurants, transport, hotels, shops, wholesalers and warehouses. The gradual restricted opening up of the economy amidst strict observance of the COVID-19 standard operating procedures improved the perceptions of doing business in Uganda. Data from Bank of Uganda indicates that total private sector credit during the current quarter increased by 4.7 percent from UGX 15.3 billion to UGX 16 billion compared to a growth of only 0.9 percent in the previous quarter. In the same vein, total exports in the current quarter increased by 63 percent to US$ 338 million from USD 207 million, in contrast to a decline of 22 percent registered in the previous quarter (January-March 2020).

Business managers interviewed expressed favourable prospects of the business environment (Figure 1). The projected promising prospects are primarily driven by the anticipated increase in business activity, sales turnover, expansion of new businesses, improvement in product prices, reduction in input costs and progress in the general business environment anticipated to emanate out of the continued opening up of the economy by Government.

The Business Climate Index by Sector

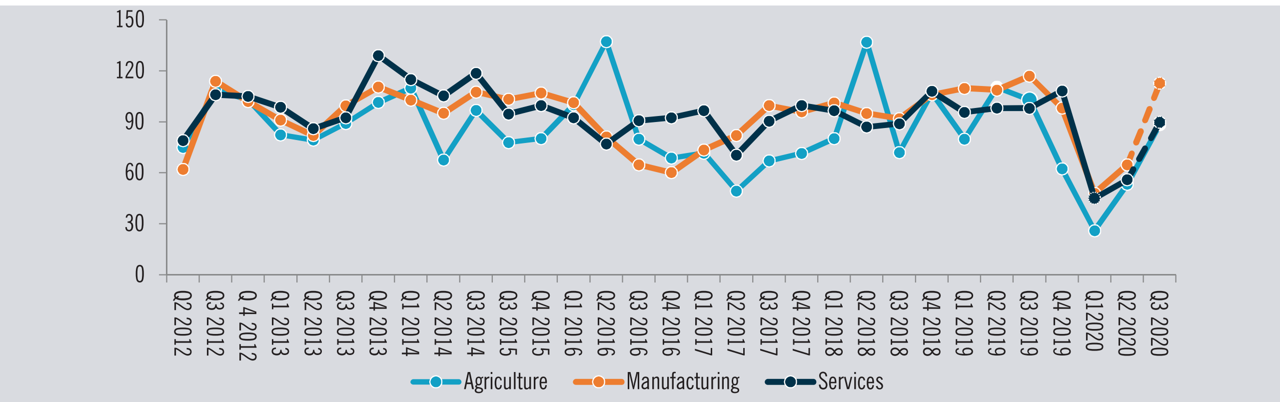
There were differences in the sectoral recovery in the business environment sentiments in the current quarter. The most remarkable improvement in business sentiments was registered in the agricultural sector, followed by the manufacturing sector, while the services sector experienced the lowest recovery (Figure 2). In the agricultural sector, sentiments for doing business improved by 27.3 points to 53.4 from 26.1 points. In the same light, the indices for manufacturing improved by 17.3 points to 64.8 from 47.5 in the previous quarter. Similarly, the index for services improved by

Figure 1 The Business Climate Assessment



Note: *Solid lines show period under review.*

Figure 2 Business Climate Index by Sector



10.7 points to 56.0 from 45.3 during the last quarter and accounted for the lowest recovery in the perceptions about the business environment. The deteriorating confidence in the service sector was primarily attributed to the less favourable input and output prices, and subdued capacity utilisation that affected business profitability.

The favourable perceptions about the business climate in the agricultural sector were primarily driven by improvements in perceptions about improved labour availability, reduced labour cost, improved business turnover and increased profit. These, in turn, helped to lift the capacity utilisation whose index improved to 40.6 in the current quarter from 11.6 in the previous quarter. Particularly, Uganda exported larger quantities of its traditional cash crops in the current quarter (April-June 2020) compared to the last quarter. In the current quarter, the country exported 60,400, 60 kg bags of coffee compared to 7,400 in the previous quarter; 1,390, 185 kg bales of cotton compared to a deficit of 10,971, 185kg bales during the last quarter and 605 MT of tea compared to a deficiency of 1,327MT registered in the previous quarter[1].

In the manufacturing sector, the business sentiment improved but remained below potential. The slight improvement in business sentiment was driven by improved prospects for business expansion, improved capacity utilisation, improved labour availability, reduced labour cost and reduced input cost. For instance, industrial power consumers will pay slightly less in the current quarter (April-June 2020) compared to the previous quarter (January -March 2020) following a reduction in end-user tariffs by the Electricity Regulatory Authority (ERA). Specifically, commercial consumers will pay UGX 645.6 from UGX 649.4, Medium Industrial Consumers, UGX 570.9 from UGX 575.2, Large Industrial Consumers, UGX 361.0 from UGX 362.4, while Extra Large Consumers will pay UGX 301.7 from UGX 302.2[2].

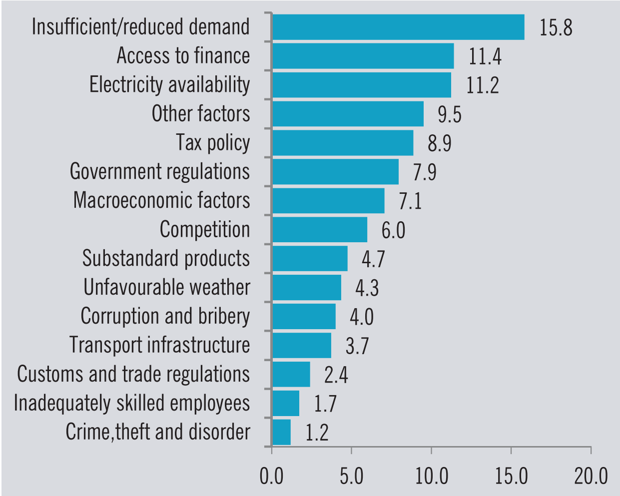
Similar to developments in the manufacturing sector, business sentiment in the services sector marginally improved on account of enhanced labour availability, business turnover, activity and improved prospects for business expansion. Nevertheless, the unfavourable input and output prices within the services sector during the quarter slowed its recovery. The registered slow recovery in the services sector emanates mainly from the negative perceptions from the hospitality sector (i.e. tourism sector). During the quarter, Uganda's airport remained closed to tourists.

Challenges in doing business

The top five most essential constraints in doing business for the current quarter were insufficient demand, limited access to business finance, electricity unavailability, tax policy and government regulation (Figure 3). The heightened burden of government regulation on business perception emanated from the restricted partial opening of the economy by Government. During the quarter, partial easing of the COVID-19 lockdown, came with strict requirements on businesses to observe Standard Operating Procedures such as the provision of handwashing equipment, sanitisers, washing soap, social distancing of customers which generally increased the cost of business operation. Concerning, electricity unavailability, during the quarter, Umeme suspended free power connections under the Government aided Electricity Connection Policy (ECP). The program aimed at subsidising last mile electricity connection to customers.

Regarding insufficient demand, the outbreak of the global pandemic led to cancelling of orders from Uganda due to port closures in some of the country's major importers. This resulted in a reduction in the demand for the country's exports which are mainly agricultural commodities and natural resources. Secondly, domestic demand has been subdued on the backdrop of limited access to personal finance. Indeed data from Bank of Uganda reveals that private sector credit for personal and household loans dipped by 2.1 percent to UGX 2.6 Billion from UGX 2.7 Billion in the current quarter. This is in contrast to a 1.4 percent growth during the same quarter in 2019.

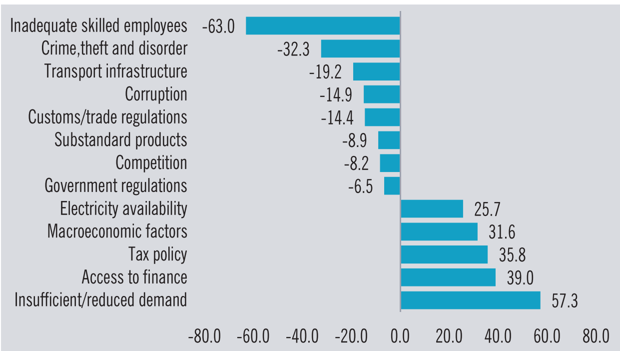
Figure 3 Business Constraints (%)



How have the business constraints evolved over the last period?

The results (Figure 4) indicate that the four most significant challenges that businesses had to deal with during the quarter are also the ones whose severity got worse. The severity of the challenges posed by insufficient demand was perceived to have been elevated during the current quarter. In particular, 71.2 percent of all business executives in our sample indicated that insufficient demand became more of a problem, 14.8 percent stated that it was unchanged. In contrast, 13.9 percent indicated that low demand was less of a problem. Unlike the previous quarter, access to finance was reported to be more of a problem in the current quarter, with more than half (56.1%) of business executives reporting its severity. Also, the severity of electricity unavailability was more pronounced in the current quarter than in the previous quarter. In particular, 51.6 percent of businesses reported that electricity inaccessibility had become more of a challenge in the current quarter. As already mentioned the suspension of the free power connections under the

Figure 4 The evolution of business constraints (% of businesses)



1 https://www.bou.or.ug/bou/bouwebsite/Statistics/Statistics.html

2 https://www.era.go.ug/index.php/media-centre/what-s-new/304-era-reduces-electricity-tariffs-for-the-second-quarter-of-2020

Government aided Electricity Connection Policy (ECP) has delayed new connections to business premises.

Future business outlook: July – September 2020

The businesses are more optimistic about the near term developments than they were in the last quarter. The expected index for July – September 2020 is 92.2 (figure 1) and is 37.2 index points higher than the current quarter's expectation which was 55 points. Generally, improvements in business conditions are expected to accelerate across all sectors and will benefit most from increased business activity, bright prospects for business expansion and favourable product prices.

However, there are sectoral differences in the expected business environment. Lower business confidence is expected in the agricultural and service sectors, while the manufacturing sector is expected to register above potential improvements. The expected indices are 88.5, 112.7, and 89.7 for agriculture, manufacturing and services respectively. While the future perceptions for doing business in the agriculture sector improved significantly (63.8) compared to the previous quarter, business perceptions in this sector are still expected to be below potential. The expected below the potential performance of agriculture sector could be attributed to the high cost of imported agricultural inputs (fertiliser and seeds) brought about by disruptions in the supply chain due to the COVID-19 pandemic restrictions. Also, the agricultural sector is likely to perform below potential owing to the onset of the effects of the El Nino with more volatile and unfavourable weather patterns during the coming quarter, implying that the gains experienced in the current quarter might not be sustained.

The expected favourable business environment in the manufacturing sector is anchored around improvements in domestic demand, product prices, capacity utilisation and incoming new business, possibly signalling business recovery after the effects of the COVID-19 pandemic lockdown.

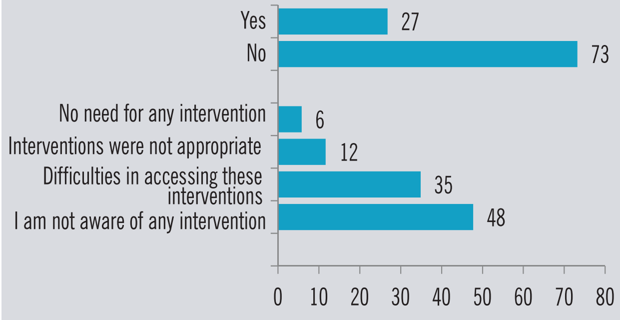
Question of the Quarter

Access to the government COVID-19 pandemic bailout for business recovery

In this quarter, we sought to understand if business owners had access to any government bailout interventions aimed at enabling their business to recover from the effects of the COVID-19 lockdown. In particular, we asked: a) "Has the business been a beneficiary of any government bailout interventions aimed at reviving businesses during and after the COVID-19 period?" b) "And if not, what are the reasons for the failure to access?"

Results indicate that majority of businesses in our sample (73 percent) had not received any bailout support from Government aimed at revitalizing their business from the effects of the lockdown. Among the firms that had not received the bailout support, 48 percent reported the lack of awareness about the available bailout interventions while 35 percent reported difficulties in accessing the available interventions. As such, the Ministry of Trade, Industries and Cooperatives needs to step-up awareness campaigns via multimedia channels as well as through physical meetings with business associations to provide information to business executives on the available bailout plan by Government. Besides, the terms, conditions and requirements for accessing the bailout need to be tailored to the structure of Ugandan businesses and be made simple to enable access.

Figure 5 Access to the government COVID-19 pandemic bailout for business recovery, %



Conclusions

Perceptions about doing business in Uganda in the current quarter (April-June 2020) improved slightly compared to the previous quarter (January-March 2020). The positive sentiment in the business environment was primarily driven by the restricted partial easing of the COVID-19 pandemic lockdown that had been instituted by Government in the previous quarter to contain the spread of the virus. Insufficient demand, limited access to finance, concerns over the cost and reliability of electricity supply and unfavourable tax policy were critical binding constraints to business competitiveness in the current quarter. Considering future expectation, business sentiment in all sectors was positive. The next quarter will see significant improvement in the performance of the manufacturing sector due to expected recovery in product prices, domestic demand, capacity utilisation, sales turnover and favourable general business environment. However, the positive sentiment in the agricultural sector is not likely to be sustained due to expected high input cost and El Nino effects.

Based on the findings, most business executives in Uganda are not aware of any government bailout interventions for business recovery from the effects of the COVID-19 lockdown. In this regard, it is vital to step up sensitisation and training of business owners about how to access the planned government bailout plan. Also, the conditions and requirements for accessing the bailout need to be made relatively straightforward to enable quick access.

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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