EPRC ECONOMIC POLICY RESEARCH CENTRE

Towards Sustainable Development

The Uganda Business Climate Index

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The Performance of the Manufacturing Sector Declines amidst a Slight Improvement in Business Sentiments

Executive Summary

The Business Climate Index (BCI) improved marginally by 4 percentage points to 91 in the current quarter (October-December 2024) from 87 in the previous quarter (July to September 2024).The slight improvement registered during the quarter was on account of reduced input cost, increased capacity utilisation, business activity, and profitability, primarily stemming from end-of-year and Christmas season business sentiments. Particularly, business sentiments within the service sector registered significant improvements of 14.8 percentage points, rising to 93 from 79 in the previous quarter based on increased sales turnover, incoming of new businesses and increased business activity. Nonetheless, sentiments in the Manufacturing sector declined by 9 percentage points to 76.9 from 85.9. The deterioration in business perceptions within the manufacturing sector is partly due to reduced capacity utilisation, low business activity, low business optimism and unfavourable product prices. Nonetheless, the near-term business sentiments (January-March 2025) indicate anticipated slight improvements in conditions for doing business from the current 91 index points to 93.5 index points. This improvement will mainly be driven by the expected advancement in the manufacturing sector. The favourable business conditions in the upcoming quarter is attributed to a projected improvement in the general business environment, lower input costs, improved product prices, and a rise in business activity spurred by the reopening of schools following the extended third-term holiday break.

Data and methods

The data used in computing the current Business Climate Index (BCI) is from a cross-sectional survey of 1,084 business establishments sampled by the Uganda Bureau of Statistics from the 2023 Uganda Revenue Authority Corporate Income Tax (CIT) database. Starting with Financial Year 2024/2025, the BCI sample was refreshed to include more firms to minimise sample bias due to business attrition over the last decade. Previously, only 200 firms, first tracked in 2012, provided the basis for BCI computation until the end of Financial Year 2023/24.

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: "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 quarter under review relative to the previous quarter and their expectations for the next quarter. Based on the business evaluation indicators explained earlier, we compute the business climate index as the weighted arithmetic means of individual business evaluation indicator indices. The indices range from 0 – 200. The interpretation of the BCI is such that scores above 100, point to an improving/above average business climate. Scores below 100, imply that the general business conditions are getting worse/below average. And a score of 100, points to unchanged business conditions.

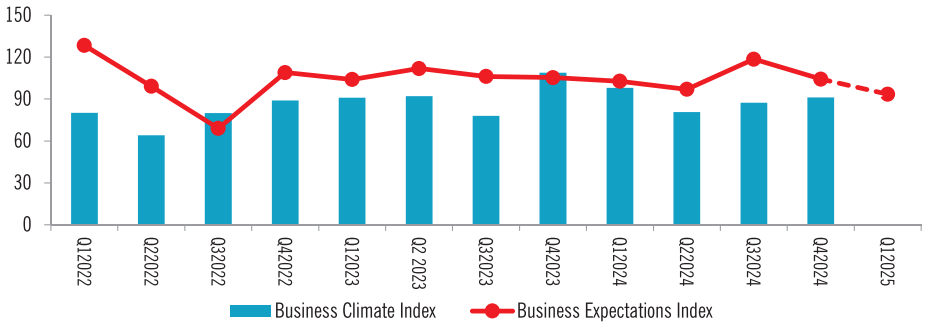
Also, the index analyses the evolution of challenges faced by businesses during October-December 2024 by identifying which business constraints became more of a problem and less of a problem. We also ask business managers to indicate how each identified business constraint has evolved during the quarter. 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 sentiments improve in the services sector, but the general business climate remains below potential and the future outlook remains optimistic.

Results indicate that the Business Climate Index improved slightly by only 4 points, to 91 during the current quarter (October-December 2024) from 87 in the preceding quarter (July-September 2024), (Figure 1). The slight improvement in the conditions for doing business resulted from the general improvement in most business indicators, specifically, profitability, improved capacity utilisation, general business environment and the entry of new businesses. The improvements in overall business sentiments were driven by the performance of the service sector, especially in the banking industry, which resulted from

Figure 1 The Business Climate Assessment



Source: BCI survey, October 2024

the reduction in lending rates.

Bank of Uganda (BoU)'s gradual easing of the monetary policy explains the reduction in the cost of credit easing as well as the strong economic performance in the preceding months. Notably, the reduction in the Central Bank Rate (CBR) in October 2024 by 25 basis points from 10 percent to 9.75 percent by the Monetary Policy Committee played a key role in the decline in lending rates hence the increase in credit demand, which boosted conditions of doing business. Indeed, statistics from BoU indicate that commercial bank credit to the private sector increased by 2.3 percent from UGX 21.2 trillion to UGX 21.7 trillion during the quarter.

The end-of-year and Christmas season's increased economic activity at the end of the quarter may have influenced positive sentiments during that period. A surge in demand for a wide range of goods and services typically accompany the festive season.

The BCI findings corroborate those of other indices, notably, Uganda Development Bank's Business Tendency Index (BTI) and the Purchasing Managers Index (PMI) by Stanbic Bank Uganda, which reported optimism about business conditions in the months of November and December 2024, partly due to the consistently higher consumer demand.

The Business Climate Index by sector

Business sentiments in the Agricultural and Service sectors show a positive trend during the quarter while the manufacturing sector shows a negative trend.

Sectoral analysis shows that the business sentiments in the service sector increased by 14.9 percentage points from 79 to 93 percentage points in the current quarter. The increase was driven by increased sales turnover, incoming of new businesses and increased business activity. This could be attributed to the reduction in the CBR, as earlier explained. Similarly, the agriculture sector registered positive business sentiments mainly on account of increased business activity, favourable input costs and incoming of new businesses partly because the quarter coincides with the planting season, making conditions favourable for farming activities.

On the other hand, business sentiments within the manufacturing sector declined by 9 percent point to 77 from 86 percentage points. The registered decline in the manufacturing sector was driven by unfavourable product prices, low-capacity utilisation, business owners' pessimism about the business environment and decline in general business activity. The negative sentiments registered in the manufacturing sector could have been on account of the depreciation of the Uganda Shilling against the US dollar. Indeed, the Uganda shilling depreciated by 0.3 percent from UGX 3,667.9 to UGX 3678.6 per US$, during October and November 2024. The marginal depreciation in the value of the shilling relative to the dollar resulted from increased demand for dollars by corporates and interbank players during the Christmas period, which outpaced the foreign exchange inflows.

Challenges in doing business.

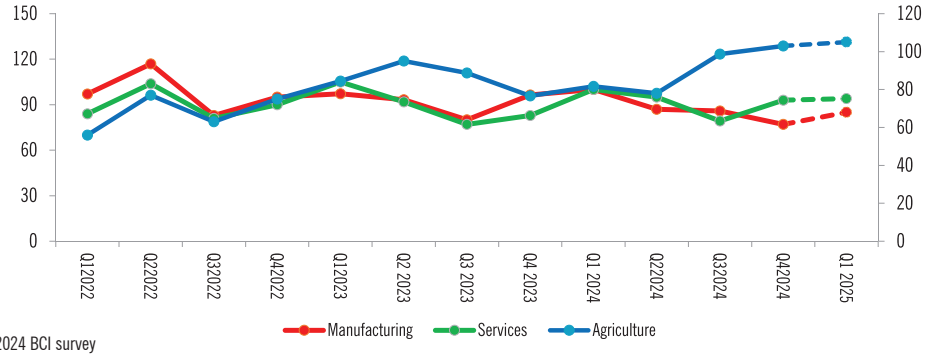
The top three most pressing constraints to doing business for the current quarter include unfavourable tax policy, increased competition from fellow businesses and unfavourable macroeconomic factors (Figure 3). Some of these factors have persisted as captured in the last quarters, implying that these business constraints are rather persistent.

The business community reported unfavourable tax policy as the main obstacle this quarter, similar to last quarter. The negative sentiments about the tax policy are mainly due to the effects of the changes in the tax laws that took effect on 1st July 2024.[1] For instance, the introduction of a withholding tax of 10% on commission paid to payment service providers, such as banking agents or other agents offering financial services. The implementation of these new tax policies has increased the cost of operation in the targeted businesses. The introduction of new taxes exacerbates the prior business concerns of multiple taxation as it adds to the existing taxes. This further increases the tax burden on businesses and potentially discourages investment.

In addition, the persistent complexity of the compliance process, characterised by bureaucratic procedures and technical challenges with digital systems, further burdens businesses. These findings corroborate those of MoFPED (2022; 2025), which emphasised the role played by

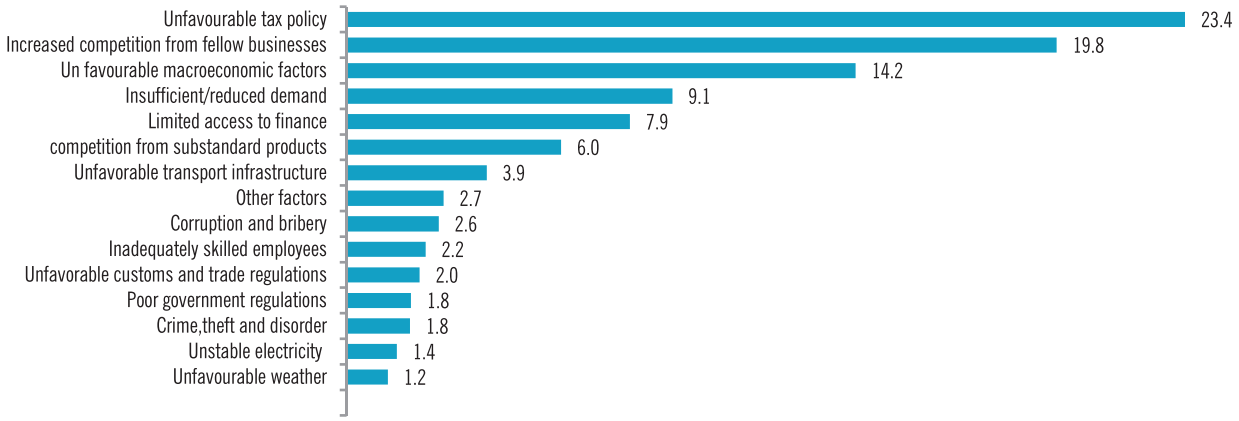
1 https://globaltaxnews.ey.com/news/2024-1719-uganda-issues-tax-amendment-acts-for-2024

Figure 2 Business Climate Index by sector



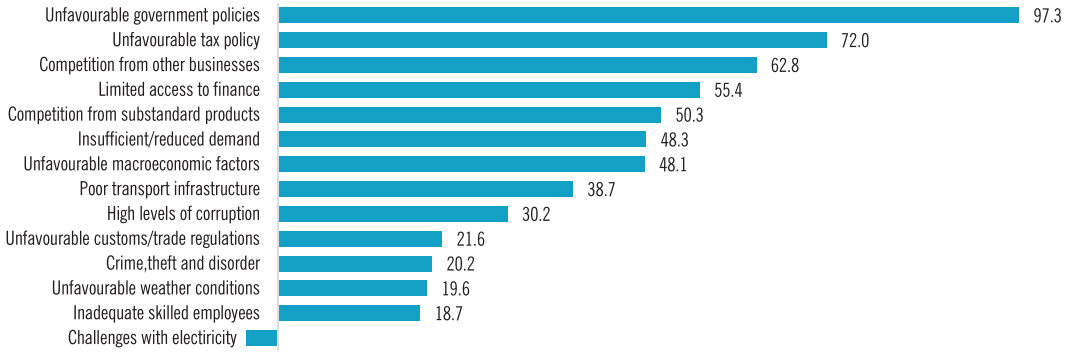
Source: October-December 2024 BCI survey

Figure 3 Business Constraints (percent)



Source: BCI survey, October-December 2024

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



Source: October-December 2024 BCI survey

the tax system in increasing the size of the informal sector by pushing the already registered and formal businesses out of formalisation.

Relatedly, the challenge of increased competition from other businesses emanates from the entry of new businesses (especially foreign ones) into the domestic market, which charge very low prices for most of their products. Additionally, the ease of entry of informal businesses into the same operating areas with the formal business also lowers sales as both categories of businesses compete for the same clientele. Worse still, consumers are more likely to buy from informal businesses as these tend to charge lower prices relative to their formal counterparts since the former do not face extra operational costs resulting from taxation (MoFPED 2022)[2]. Regarding the unfavourable macroeconomic factors, as explained earlier, the depreciation of the exchange rate during the quarter made conditions unfavourable for doing business, especially for importers.

The evolution of business constraints

During the quarter October to December 2024, Uganda's business environment faced multiple structural and policy-related challenges that intensified compared to the previous quarter. The most pressing issues included perceived unfavourable government policies, mainly tax policies, which continued to dampen business sentiments. Businesses cited frequent and unpredictable changes in regulations, as well as complex compliance requirements, which increase operational costs and create uncertainty for investors.

Additionally, the tax burden-characterised by high rates and inadequate tax incentives for small and medium enterprises (SMEs)-has remained a critical concern, limiting both profitability and reinvestment potential. This aligns with findings by the EPRC in 2023 which highlighted persistent taxpayer dissatisfaction related to the complexity of tax administration and perceived inequities in the tax system.[3]

Moreover, increased competition, both from local players and imported goods, has lowered profit margins across businesses. Notably, competition from substandard products-often cheaply imported, undermines quality-conscious businesses and erodes consumer trust. These challenges and many others partly explain the premature collapse of businesses in Uganda, which leads not only to a loss in government revenue but also to the erosion of vital sources of livelihood for many individuals and families.

Notably, while these challenges became more pronounced during this period, they are not new; rather, they represent a continuation of structural weaknesses identified in the previous quarter, indicating persistent vulnerabilities in Uganda's business climate that require targeted and consistent policy intervention.

Future business outlook: January-March 2025

Businesses are optimistic about near-term developments, but business sentiments are still below potential. Figure 1 projects that business sentiments will improve by 2 index points, reaching 93 index points in the next quarter (January-March 2025), from the current 91 index points. This expected improvement in business perceptions is anticipated to emanate from the expected reduction in input prices, favourable product prices, and overall improvement in the business environment.

2 https://eprcug.org/publication/assessment-of-informal-businesses-in-uganda/

3 https://eprcug.org/publication/actionable-tax-compliance-in-uganda-lessons-from-other-countries/?filename=Actionable+Tax+Compliance+in+Uganda+Lessons+from+other+countries.pdf&ind=1686579458127&refresh=64f3ec11c773d1693707281&wpdmdl=15938

Similarly, business perceptions across the three sectors indicate positive business sentiments about the future. Sentiments across all three sectors are expected to improve from index points 103 to 105 for agriculture; 77 to 85 for manufacturing and 93 to 94 for service in the next quarter (January - March 2025) — see Figure 2. Anticipated enhancements in the business environment, largely driven by the reopening of schools following the long third-term holiday, account for the expected improvement across the three main sectors. Higher sales turnover usually accompanies school reopening across all sectors, which points to an increase in production in preparation for the expected rise in demand as children report back to school. Furthermore, the upcoming quarter coincides with the harvest season, which accounts for the expected stability in inflation during that period.

Question of the quarter

Effect of the beginning of campaigns for the 2026 elections on businesses

In this quarter, we sought to understand how the expected kick off of campaigns for 2026 national elections could potentially affect the business environment. Particularly, we asked: *(i) "Do you expect businesses to be affected by the campaigns for the 2026 elections that will kick off in 2025?" (ii) "If Yes, how?"*

Results presented in Figure 5 indicate businesses' expectations regarding the effect of the 2026 election campaigns, which are expected to begin in the first quarter of 2025. Almost four in every ten businesses expect a disruption in their business operations when the campaigns for the 2026 national elections start in 2025.

Among the concerns raised, the most prevalent is the potential reduction in operating hours due to security risks (35 percent, highlighting worries about possible unrest or curfews that could limit business activity). Furthermore, businesses expect a general increase in prices of goods and services (34 percent), which reflects fears of inflationary pressures often associated with election periods due to increased political spending.

Additionally, 25 percent expect a reduction in demand, driven by security concerns, signaling that consumer spending may decline as people avoid crowded places or reduce non-essential purchases amidst uncertainty. The service sector, specifically the tourism industry, expects a great reduction in demand due to security and safety concerns.

Overall, the results suggest that while not all businesses anticipate negative impacts, there is notable anxiety about the indirect consequences of political campaigns, especially around security and inflation. These insights highlight the importance of proactive measures to maintain stability during the election period, as business confidence is a key driver of economic resilience.

Conclusion

Conditions for doing business in Uganda in the current quarter (October-December 2024) slightly increased to 91 index points compared to the previous quarter, though the general business environment stayed below potential. The performance registered during the quarter was driven by a favourable general business environment, reduction in input costs, increased capacity utilisation and business activity. The improvement in these indicators could partly be explained by the central bank's reduction in the cost of credit and the festive season at the end of the year. This underscores the role played by increased access to cheap credit in business operations.

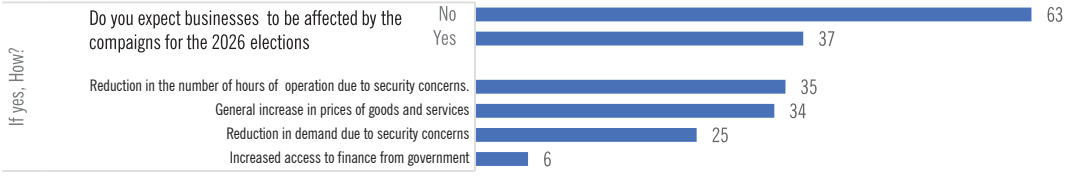
At the sectoral level, analysis shows that the business sentiments in the service sector increased by 14.9 percentage points from 79 to 93 percentage points in the current quarter. Similarly, the agriculture sector registered positive business sentiments. On the other hand, business sentiments within the manufacturing sector declined by 9 percent to 77 points from 86 percentage points.

In addition to being top challenges for the quarter, the severity of tax policy continued to worsen, mainly due to some of the tax laws that were implemented effective 1st July 2024. The recurring nature of tax-related challenges each quarter highlights the need to strike a balance between tax policy and business sustainability. This will significantly contribute to sustained tax revenue collection while preserving vital sources of livelihood for the population by ensuring business survival.

Near-term business sentiments suggest business conditions should improve slightly next quarter. The three main sectors similarly express optimism, implying a positive business outlook for the January-March 2025 quarter. This anticipated improvement in business sentiments is because the forthcoming quarter coincides with both the harvest season and the reopening of schools for the first term, 2025.

Findings from the question of the quarter indicate that about 4 in 10 businesses expect disruptions from the campaigns for the 2026 national elections which are expected to begin in 2025. Businesses expect a reduction in operating hours due to security risks and inflationary pressures often associated with increased government expenditure during campaigns. Additionally, businesses expect a reduction in demand due to security concerns, especially in the service sector. As such, there is a need to ensure the stability of the economy during the campaign period for the 2026 national elections, given the role played by businesses in Uganda.

Figure 5 Effect of election campaigns on local businesses



Source: October-December 2024 BCI survey

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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