

Disruptions from the second COVID-19 lockdown affect the business environment, and the future outlook remains downcast.



Photo: Some of the closed arcades at Luwum Street in Kampala during the second lockdown.

Photo: EPRC, 2021.

Abstract

The Business Climate Index (BCI) remained below potential for the sixth consecutive quarter since the 2020 first quarter (January-March 2020). Nonetheless, business perceptions in the current quarter (April-June 2021) improved slightly by 5 basis points from 51 in the previous quarter (January-March 2021) to 56 in the current quarter (April-June 2021). The below-potential performance in business sentiments was primarily driven by the unfavourable business environment, low product prices and business activity during the second lockdown. In particular, the new adjustments in curfew hours, the ban on weekly markets and transport restrictions disrupted the business operations in the current quarter. Meanwhile, business perceptions in the agriculture sector subdued more compared to manufacturing and service sectors. This was on a backdrop of a less favourable business environment, lower product prices, turnover, profit, and reduced capacity utilisation. Perceptions about business sentiments in the next quarter (July-September 2021) are pessimistic because of the anticipated decline in business activity, turnover, labour availability and inability to expand and/or start-up new businesses.

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 157 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 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 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 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 Perceptions slightly improved, but future sentiment further deteriorated.

Results indicate a slight improvement in the conditions for doing business in the current quarter (April – June 2021), having improved from a generally pessimistic trend over the previous five quarters—since the first quarter 2020 (January- March 2020) (Figure 1). The business climate index is 56 and has slightly improved by 5 index points on a quarter-on-quarter basis from 51 during (January–March 2021). Despite the slight improvement in the conditions for doing business in Uganda during the period under review, all sub-indices, namely business activity, profits, turnover, business environment, and start-up of new businesses, were all below potential (below 100). This indicates that, like the previous quarter (January –March 2021), the economy is operating at less than full potential.

The below potential performance in the business environment was driven mainly by the re-institution of the second lockdown in June 2021 due to a surge in the number of COVID-19 cases. In particular, the re-suspension of public transport, unfavourable adjustments in curfew hours, the suspension of weekly markets for agricultural produce, and the closure of schools in the second wave of the pandemic elevated the perceived risks for doing business in the current quarter. In addition, insufficient demand, unfavourable tax policy, unfavourable macroeconomic factors and increased difficulty accessing reliable and cheap electricity continued to be the binding constraints to business competitiveness. It was reported to be more of a problem in the current period.

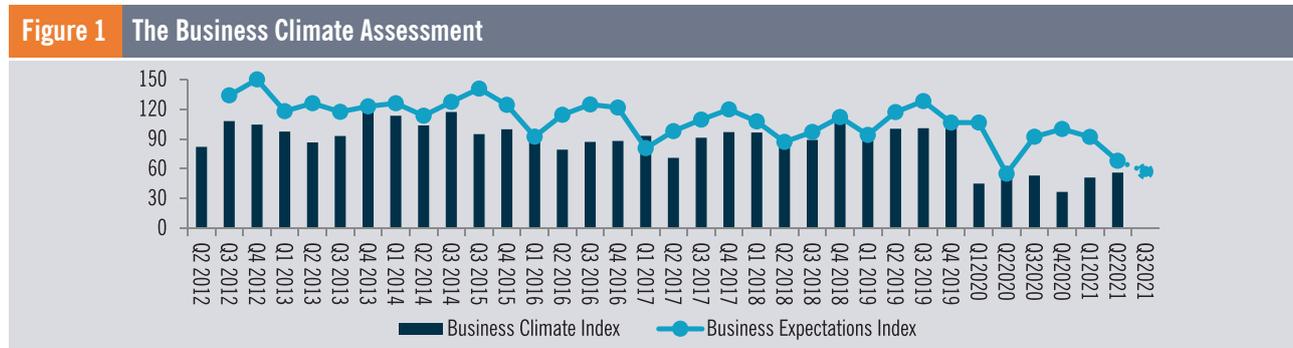
Indeed, by the end of May 2021, the government announced the second lockdown, which resulted in the closure of businesses and job losses

which lowered the purchasing power amongst consumers. Besides, in April 2021, the government passed new taxes to raise revenues. For instance, under the Excise Duty Amendment Bill, 2021, which Parliament endorsed, motorists were required to pay an additional UGX 100 tax per litre of petrol and diesel. Furthermore, effective April 2021, the government extended the requirement to fix Digital Tax Stamps to imported and locally manufactured cement and sugar. In addition, the appreciation of the Uganda shilling against the leading world currencies has affected business, especially in the agricultural sector, which accounts for the largest share of the country’s exports. For example, the shilling appreciated by 0.3 percent against the United States dollar (USD), trading at an average mid-rate of UGX 3,540 per USD in June 2021 from UGX 3,553 per USD in May 2021.¹

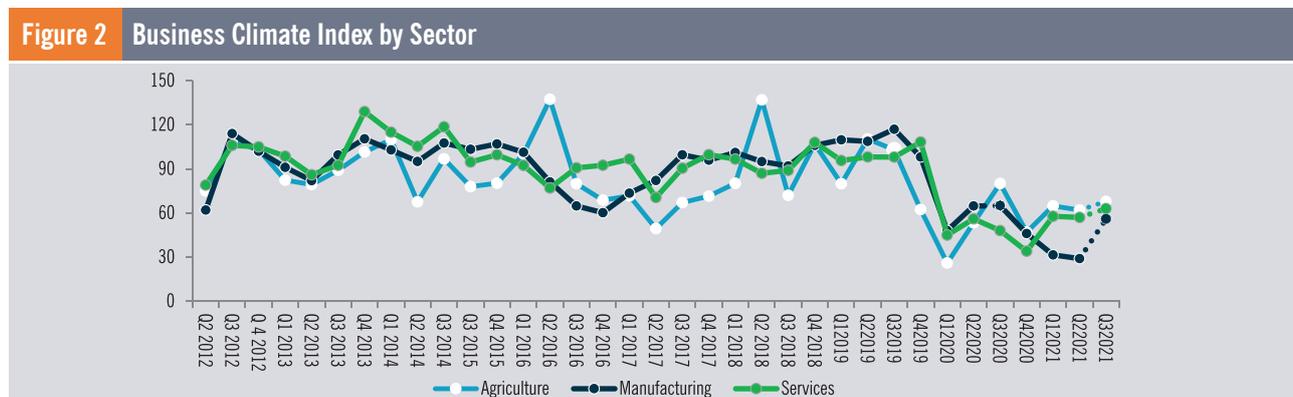
The Business Climate Index by Sector

While perceptions in all the three sectors (agriculture, manufacturing, and services) subdued, business perceptions in the agriculture sector dampened more relative to the manufacturing and service sectors during the current quarter (April-June 2021) (Figure 2). In this regard, the agriculture sector relapsed by 3.3 points to 61.5 from 64.8 points registered in the previous quarter. On the other hand, the manufacturing sector decreased by 2.2 points to 29.3 from 31.5 points registered during the last quarter. Similarly, the service sector declined by 0.7 points to 57.1 from 57.8 points in the previous quarter (January-March 2021). The increased deterioration of business perceptions in the agriculture sector in the current quarter was primarily attributed to the low prices for agricultural produce, unfavourable business environment, pessimism within the business community and low-capacity utilisation. Similarly, business sentiments in the manufacturing and services sectors declined during the current quarter compared to the previous quarter because of low product prices, unfavourable business environment, low profits, fall in business activity, among others. The re-institution of the second lockdown could have amplified the decline

1 https://www.finance.go.ug/sites/default/files/Publications/POE-2021-06-JUN_0.pdf



Source: EPRC survey July 2021



Solid lines show period under review.

Source: EPRC survey July 2021

in the performance of the three sectors as a result of the outbreak of the second wave of COVID-19 in May 2021.

Challenges in doing business

Like the previous quarter (January-March 2021), the top five most important constraints in doing business for the current quarter comprised increased government regulation and insufficient demand. This was in addition to the persistent business challenges (electricity unavailability, unfavourable tax policy, macroeconomic factors, and inadequate demand). These have not changed since last quarter. This suggests that major policy and regulatory constraints facing Ugandan businesses are rather persistent. The increased government regulation in the current quarter could have emanated out of the need to adhere to the COVID-19 standard operating procedures to contain the outbreak of the second wave of the pandemic. In addition, macroeconomic factors, notably exchange rate volatility and challenges with electricity availability continue to be the major business constraint in the current quarter.

Just like in the previous quarter, the persistent burden of insufficient demand emanated from the low purchasing power in the economy due to severe job losses caused by the second wave of the COVID-19 pandemic. Additionally, an increase in precautionary savings due to the rising uncertainties regarding income flows² in preparation for future lockdowns also heightened the challenge of insufficient demand. Again, tax payment has continued to be burdensome on businesses since their capacity to meet tax obligations continues to be severely affected by the low business performance resulting from COVID-19 and its containment measures.

² <https://www.bou.or.ug/bou/bouwebsite/bouwebsitecontent/publications/StateofEconomy/publications/StateOfEconomyReports/2020/Sep/State-of-the-Economy-September-2020.pdf>

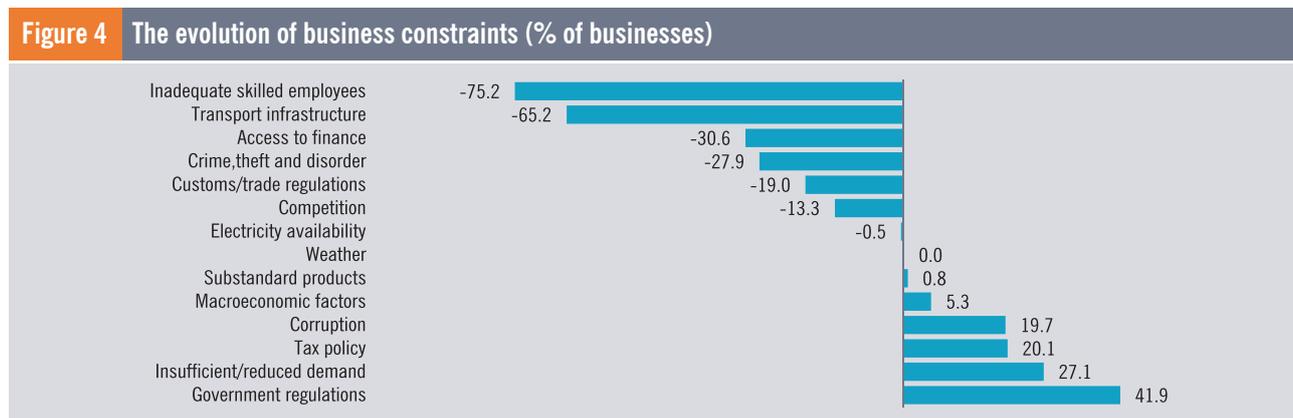
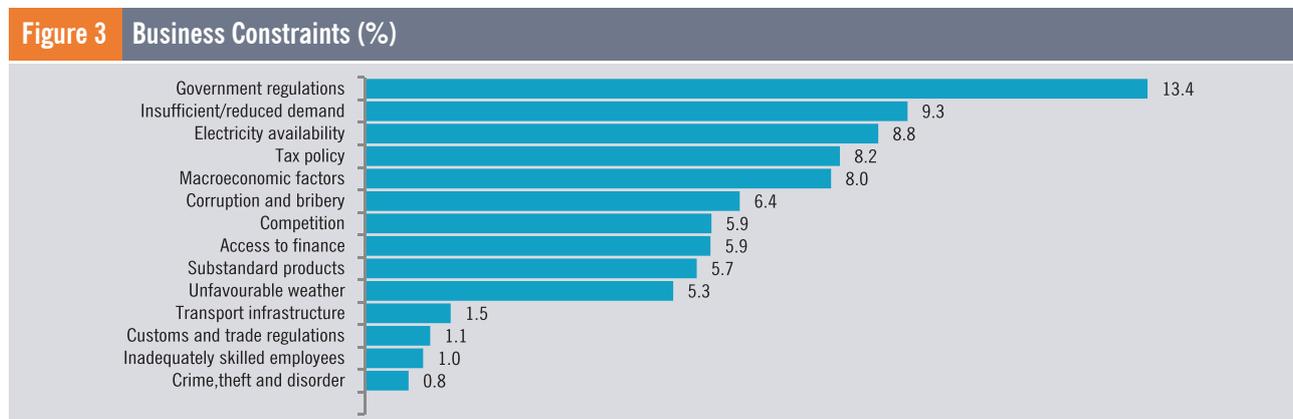
How have the business constraints evolved over the last period?

The results (Figure 4) indicate that some of the most important challenges that businesses had to deal with during the current quarter are also the ones whose severity got worse over the current quarter. Unlike in the last quarter (January-March 2021), the severity of the challenges posed by increased government regulation and insufficient demand were perceived to have been elevated during the current quarter. Additionally, tax policy was also reported to be more of a problem in the current quarter as in the previous, due to a severe decline in the capacity of businesses to meet their tax obligations due to the subdued demand and sales turnover. Lastly, unlike in the previous quarter, increased corruption and unfavourable macroeconomic factors were serious concerns within the business community, with high severity during the current quarter.

Future business outlook: July – September 2021

Like the previous quarter, businesses continue to be pessimistic about the near term developments. The expected index for July – September 2021 is 57 (Figure 1) and is 10.9 index points lower than the current quarter's expectation which is 67.9 points. Generally, further deterioration in business condition is expected to relapse most from anticipated reduced business activity, turnover, inability to expand/start up new businesses and increase in labour scarcity, heightened by the disruptions due to the COVID-19 pandemic and the uncertainties from expectations of subsequent COVID-19 waves.

Nonetheless, sectoral differences in the expected business environment exist. In this regard, lower business confidence is expected in the manufacturing and service sectors compared to the agriculture sector. In particular, the manufacturing sector is anticipated to suffer more than the service sector, while the agriculture sector is expected to have a relatively modest decline. The expected indices are 67.9, 55.7 and 63 for agriculture, manufacturing and services, respectively. The



anticipated slightly favourable sentiments for doing business in the agriculture sector are attributable to the anticipated improvement in labour availability, business environment, business optimism, business turnover, and better product prices.

On the contrary, the expected unfavourable business environment in manufacturing sectors is anchored around the anticipated deterioration of the general activity, turnover, reduction in capacity utilisation, and inability to expand new business operations, possibly signalling business risks associated with the expected future lockdowns.

Question of the Quarter

Ability to operate business activities from home

In this quarter, we sought to understand if business owners and their workers could operate business activities from home, given the reinstated lockdown restrictions.

In particular, we asked: a) “Have you and your workers been able to operate business activities from home, given the reinstated lockdown restrictions?” b) “If No, what is the main reason for the failure to operate business activities from home?”

Results (Figure 5) indicate that most businesses in our sample (84 percent) were able to operate business activities from home during the reinstated lockdown.

Among the firms that were unable to operate business activities from home, 40 percent of those reported that their work requires physical presence at the premises, 30 reported that they lacked skills to operate work-from-home equipment such as computers and 21 percent reported that they lacked funds to facilitate their workers to work from home. The results reveal the need for government to subsidise work-from-home equipment such as computers to make them affordable to business owners. The government could also support capacity-building activities

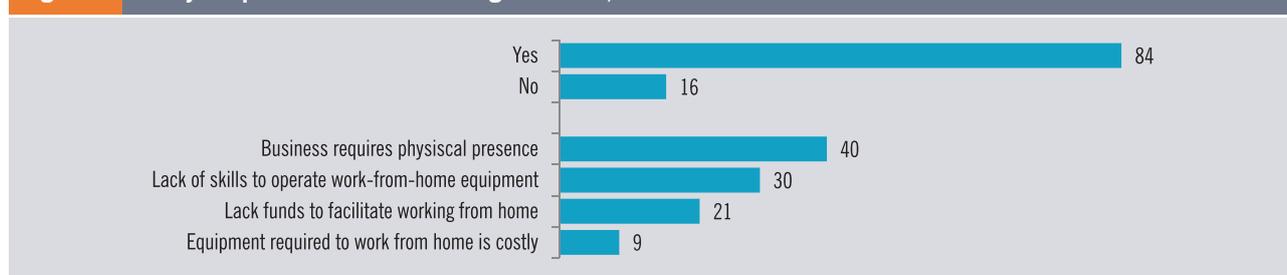
related to work-from-home equipment such as computer training within the business community.

Conclusion

Perceptions about doing business in Uganda in the current quarter (April-June 2021) slightly improved compared to the previous quarter (January-March 2021). Despite the slight improvement in the conditions for doing business, all sub-indices, namely business activity, profits, turnover, business environment and start-up of new businesses, among others, were all below potential (below 100), reflecting disruptions caused by the outbreak of the second wave of COVID-19 pandemic that resulted into the re-institution of the second lockdown.

Just like in the last quarter, some business constraints persisted. In this regard, increased government regulations, insufficient demand, unreliable electricity, unfavourable tax policy, and exchange rate volatility were critical binding constraints to business competitiveness in the current quarter (April-June 2021). Considering future expectations, business sentiments for the next quarter (July-September 2021) will further deteriorate across all sectors. The next quarter will see below-potential sentiments for all the sectors, with the lowest expectations in the manufacturing sector. The expected unfavourable business environment in the manufacturing sector is anchored around anticipated deterioration of the general activity, turnover, reduction in capacity utilisation, and inability to expand new business operations, possibly signalling business risks associated with the expected future lockdowns. Considering the ability to operate business activities from home, some business executives and their workers could not work from home during the reinstated lockdown. The government must subsidise work-from-home equipment such as computers to make them affordable to business owners. In addition, the government could also support capacity-building activities related to work-from-home equipment such as computer training within the business community across the country.

Figure 5 Ability to operate from home during lockdown, %



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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Acknowledgement

The Business Climate Survey team appreciates the support received from all participating business establishments across the country, our partners at the Uganda National Chamber of Commerce and Industry, Kampala City Traders Association and all persons who reviewed and edited this publication.

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