POLICY WORKSHOP ON HIGH COMMODITY PRICES

OPENING REMARKS BY HON. MINISTER OF STATE FOR FINANCE, PLANNING AND ECONOMIC DEVELOPMENT (GENERAL DUTIES)
SERENA HOTEL KAMPALA, 25TH MAY 2022

Hon. Members of Parliament Present;

The Permanent Secretary/ Secretary to the Treasury

The Deputy Governer, Bank of Uganda

The IMF and World Bank Representatives in Uganda

Other Development Partners Present

Members of the Private Sector and Civil Society

Distinguished Participants,

Ladies and Gentlemen

1. I am honoured to preside over this policy workshop that is going to deliberate on the topical issue of the rising prices of essential commodities in the country, their effects on household welfare, and the Government policy interventions and strategies to sustainably deal with the socio-economic challenges.
2. Before I dwell on the subject of the high commodity prices, allow me to provide some highlights on the recent performance of the economy.

a. Economic growth this financial year is projected at 3.8% to 4.5%, with a positive outlook in the medium term where the growth is projected at between 6 and 6.5% per annum. The positive outlook is driven by a roaring manufacturing sector, full re-opening of the economy, increased production and productivity in agriculture built around the Parish Development Model, the continued government investment in infrastructure such as roads, energy, industrial parks, growth in ICT sector, and oil production related activities.

b. Headline inflation was 4.9% for the year ending April 2022. However, this was below the policy target of 5% per annum. The increase in the inflation rate was due to a combination of supply and demand factors that continued to affect prices in April 2022. I will talk more about this later.

c. There was an improvement in the level of economic activity according to the Purchasing Managers' Index (PMI) and Composite Index of Economic Activity (CIEA). Investors' sentiments about doing business in Uganda remained positive in April 2022 as illustrated by the Business Tendency Index (BTI), which remained above the indicative threshold of 50 at 56.4 in April 2022.

d. Last month, the Shilling strengthened against the US Dollar, appreciating by 1.3% to a monthly average of Shs. 3,541.5/USD from Shs. 3,589.8/USD recorded the previous month. This appreciation was on account of higher dollar inflows, especially foreign portfolio investors.

e. Interest rates on Government securities (Treasury Bills and Bonds) have declined in April 2022, partly on account of a decrease in Government borrowing requirement.

f. Whereas we had projected a shortfall in domestic revenue of about Shs 1.5 Trillion this year, I am happy to report that the cumulative shortfall as of April 2022 was Shs 787 billion.

3. These indicators I have mentioned show that the economy is picking momentum on its recovery path from the effects of the Covid19 pandemic.

Trends in Domestic, Regional and International Inflation

4. Back to the main focus of the discussion today, until recently domestic prices and inflation in Uganda have been low. The headline inflation has averaged 3.9% between financial years 2012/13 and 2021/22; a 10-year period.

5. However, in recent months there has been a significant increase in prices for some of the essential commodities and services.

6. These include laundry bar soap, fuel (petrol and diesel), cooking oil, some food crop items (especially wheat), education services, and building materials (cement and steel), among others. As a result, the overall annual inflation has increased considerably from 2.7 percent in January 2022 to 4.9% in April 2022.

7. Accordingly, the Government has faced pressure to intervene and bring down the prices, including suggestions to remove or reduce taxes and to provide subsidies.

8. It should be noted that inflation has risen everywhere in the world including in advanced countries, emerging economies, and Uganda's peers – the developing countries.

9. For example, annual inflation rate in the US accelerated to 8.5% in March of 2022, the highest they have recorded in 40 years, before reducing slightly to 8.3% in April.

10. In United Kingdom, inflation increased to 9% in last month (April 2022), the highest they have recorded since January 1989.

11. Likewise, prices have increased in several of the middle-income emerging economies such as Brazil (12.1%) and India (7.8%), as well as in developing countries such as Ethiopia (36.6%), Rwanda (10.5%), Kenya (6.5%), among others. Therefore, despite this rapid increase Uganda's inflation (at 4.9% last in April this year) is still among the lowest in the region and the world.

12. That said, however, information from the Uganda Bureau of Statistics (UBOS) shows that prices of some essential commodities have increased rapidly and caused discomfort among sections of Ugandans.

13. In particular cooking oil prices have increased by 44% in the past one year to April 2022. The price of laundry bar soap has increased by 87% in the past one year, while fuel (diesel) price has risen by 38% during the past one year. Petrol price has increased by 35.8% and sugar price has increased by 13.6% in the past one year.

What exactly has caused the recent increase in the prices of essential commodities?

14. The causes of the recent increase in the prices of essential commodities are as follows:

a) First, the effect of COVID-19 restrictions across the world disrupted supply-chains leading to higher transport costs and shortage of intermediate raw materials used to produce items such as laundry bar soap, cooking oil and others. In the recent past, global economy has faced high shipping costs, a shortage of shipping containers, and higher fuel prices; all together leading to supply shortages globally. For example, shipping cost per 20-feet container from Shanghai to Mombasa has increased from USD 3,050 (UShs. 10.9 million) in 2020 to USD 6,100 (Ushs. 21.9 million). These costs have been passed on to consumers in the form of higher.

b) Secondly, the full opening of economies globally following relative containment of COVID-19 has led to a rapid rise in aggregate demand for a number of fast-moving-goods beginning with oil, yet production levels had been constrained by COVID-19 restrictions as shown in (a) above. A combination of the two has led to increase in prices everywhere in the world.

c) Lastly, the situation has been worsened by the Russia-Ukraine conflict which has further disrupted supply of oil, cereals such as wheat, maize, and sunflower oil, as well as essential metals like aluminum and nickel. The two countries are major producers and exporters of these commodities.

What is Government doing from the fiscal side to address the problem?

15. When prices increased a section of people including key opinion leaders and civil society exerted pressure to Government to intervene by suggesting a number of options including removal or reduction of taxes on the affected items, and provision of subsidies such as oil subsidies to bring down the prices.

16. The Ministry of Finance, Planning and Economic Development made a comprehensive analysis of the implications of these suggestions.

17. Here are some of the highlights from the analysis:

a) The tax contribution to the final price for the eight (8) key essential goods whose prices have increased rapidly (i.e., *cooking oil, soap, sugar, wheat flour, maize flour, fuel (petrol, diesel and kerosene), cement and steel*) ranges from 6.7% for kerosene to 27% for petrol, with the others having an average tax contribution of 19.7%. This clearly shows that taxes are not the main cause of the price increase.

b) The projected total revenue from these selected key consumer goods is **UShs. 4.52 trillion**, which is 18% of the projected total revenue collection for FY 2021/22.

c) Any temporary benefits that would accrue from tax reduction in an environment of increasing prices caused by external factors would cause self-reinforcing price increases if consumers decide to buy more (or even hoard) the goods whose prices would have reduced following a tax reduction. This has been evident in case of fuel subsidies in some of the neighbouring countries. The benefit is soon lost and yet the Treasury loses the badly needed revenue to provide social services and facilitate development.

18. We have also stayed away from subsidies because they are neither efficient at targeting the intended beneficiaries nor sustainable. Subsidies tend to result into what economists call a zero-sum game (*i.e., some people gaining the equivalent of other people's loss such that the net change in benefit will be zero*).

19. Research on expenditure in a number of African countries that used subsidies in the past shows that the rich benefit more than poorer households from any subsidy on products such as fuel and other fast-moving goods.

20. The increase in prices of essential commodities is a temporary one, and prices will soon normalise. For example:

a) Although the price of cement had reached Shs. 38,000 by the start of April 2022, it has dropped significantly to Shs. 31,000 by mid-May 2022. It is projected to reduce even further as the supply of imported clinker which had been disrupted by Covid-19 increases.

b) The price of a laundry bar soap has also reduced from Shs. 10,000 (which was mainly a result of hoarding) to an average of Shs. 6,300.

c) Ocean freight charges have also started to reduce. For example, the freight charges for a 20-feet container from Shanghai China to Mombasa has reduced from a peak of USD 6,100 in December 2021 to USD 2,950. The charges for the 40-foot container have also reduced from USD 9,400 to USD 5,650. This reduction in transport costs will eventually translate into reduced domestic prices.

d) In the financial year 2011/12, we faced high inflation in the region because of the drought that caused food prices to increase significantly. Inflation reached a peak of 24.4% in November 2011. Some leaders incited the public to engage in "walk-to-work" protests. The Government resisted the pressure to implement distortionary policies and instead concentrated on implementing appropriate prudent fiscal and monetary policies. In a few months the overall inflation had dropped to below 5% per year, our target inflation rate.

21. This demonstrates the need to be patient as the supply constraints that have led to global shortages abate. This will be important to avoid policy measures that could lead to long-term distortions in the economy. It is therefore important that we continue to maintain sound fiscal and monetary policies, while working to increase our production capacity to take advantage of the crisis.

22. **In conclusion, therefore, from the fiscal policy side Government is going to continue doing the following:**

a) Supporting farmers to grow more fast-maturing food and oil seeds to ensure sufficient domestic supply as well as take advantage of the rising global and regional prices to boost our export earnings. Government is scaling-up production of oil palm, sunflower and soya beans to ensure sufficient domestic supply.

b) Maintaining a competitive environment to support a continuous supply of the goods and services whose stream is currently constrained. This is intended to ensure that demand does not outstrip supply.

c) Working with the private sector to expedite alternative fuel import routes across Lake Victoria, to avoid unnecessary supply disruptions during the election season in Kenya.

d) Using appropriate fiscal and monetary policies to mitigate the impact of price shocks.

e) In the medium term, we shall construct additional fuel storage infrastructure and stock them with fuel to provide for strategic reserves to cushion consumers from effects of fuel supply shocks.

f) Expediting implementation of project activities to ensure timely start of oil production as well as development of an oil refinery.

g) Continuing to support the citizens and businesses to recover their sources of livelihoods from the impact of the COVID-19 pandemic so that they can withstand such shocks, using funds such as EMYOOGA, Small Business Recovery Fund, Microfinance Support Centre, UDB, and funding under the Financial Inclusion Pillar of the Parish Development Model.

23. Fellow Ugandans, in short, temporary solutions aimed at addressing external shocks for which the Government has little or no control can lead to long-term and painful distortions in the economy. We should avoid them and instead concentrate on fully recovering the economy and increase the domestic production capacity in the economy.

24. Ladies and Gentlemen, with these highlights on the economy and policy responses to the high prices of essential commodities, I now have the honour to officially open this Policy Workshop. Please have candid but informed deliberations. The recommendations should help to inform Government decisions to overcome the challenges we face today.

Thank you for listening.