COVID-19 and Ugandan SMEs: Impacts and speed of recovery

Livia Alfonsi, Oriana Bandiera, Vittorio Bassi, Robin Burgess, Imran Rasul, Ottavia Anna Veroux, and Anna Vitali

- This policy brief documents the impact of the COVID-19 lockdown and related economic restrictions on small and medium enterprises (SMEs) in Uganda using information on over 3,900 firms interviewed twice in the year after the onset of the pandemic.
- The survey shows that most firms re-opened soon after the spring 2020 lockdown was lifted, but they mostly did so at reduced capacity.
- One year after the start of the pandemic, revenues and profits are still 19% and 36% lower than in the pre-lockdown period.
- Low demand and lack of liquidity are still reported as main challenges by firm owners one year after the onset of the pandemic.
- Firm owners indicate interest rate subsidies, tax cuts, and unconditional cash transfers as the policy support that they would need the most.
- Policies that can boost the spending power of customers and facilitate liquidity access for firms will be critical to ensure that firms can remain open and keep paying their employees in the path to recover.

POLICY BRIEF UGA-20273

OCTOBER 2021

This project was funded by IGC Uganda

www.theigc.org

DIRECTED BY

FUNDED BY

Background

In response to the global spread of COVID-19, at the end of March 2020 the Government of Uganda announced school closures, a nation-wide lockdown on all non-essential businesses, the ban of all movements within and across districts, and a stringent night curfew. These measures, initially planned for two weeks, were extended several times: while the total lockdown was lifted at the end of May, schools remained closed and the curfew in place throughout 2020 and 2021. A second total lockdown - less strict than the previous and lasting one month - was put in place in July 2021 in response to a second wave of COVID-19 infections.

We report the findings of two phone surveys of 3,900 Ugandan firms that were fielded to study how the COVID-19 shock and related economics restrictions affected firm survival and performance in the year after the onset of the crisis.

Data and methodology

The sample includes 3,961 small and medium enterprises located in all regions of Uganda and operating in one of the following sectors: hairdressing, tailoring, welding, motor-mechanics, catering, electrical wiring, construction, plumbing. The firms were initially recruited as part of an earlier study (Alfonsi et al. 2020) and tracked yearly between 2013 and 2017.

This sample of firms was interviewed two more times in November 2020 and May 2021 using phone surveys, thanks to funding from PEDL and UCL. We interviewed firm owners with the aim of collecting information on firm characteristics, operations, and performance in the months prior to the survey. This allows us to measure firm outcomes: (i) immediately before the crisis; (ii) following the onset of the crisis up until the time of the survey.

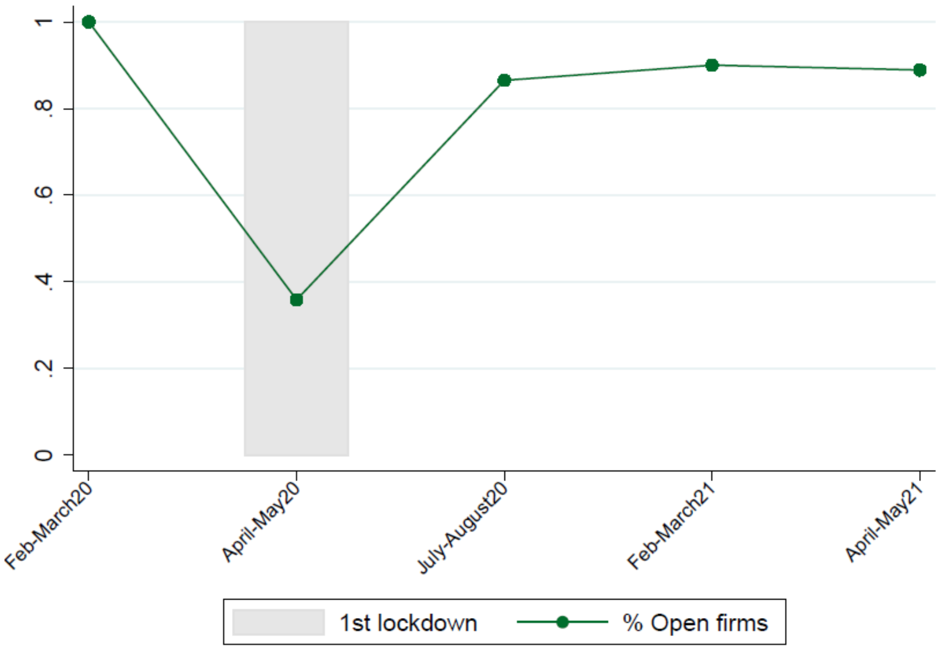
Results

1. Most firms quickly reopened after the lockdown but did so at reduced capacity.

Although only 36% of the firms in the sample stayed open during the first lockdown, immediately after the restrictions were lifted the share of open firms raised to 87%. As the economy recovered, the share of operating firms remained fairly constant: one year after the first lockdown, 89% of firms were still open (Figure 1). Nevertheless, the majority of these firms declared to be operating at reduced capacity because of reduced hours of operation (60%), workforce (39%) or machines usage (20%).

This suggests that, although the pandemic had a modest effect on firms' closures, it significantly reduced their operations such that after one year most businesses have not yet fully recovered.

Figure 1: Firm closures

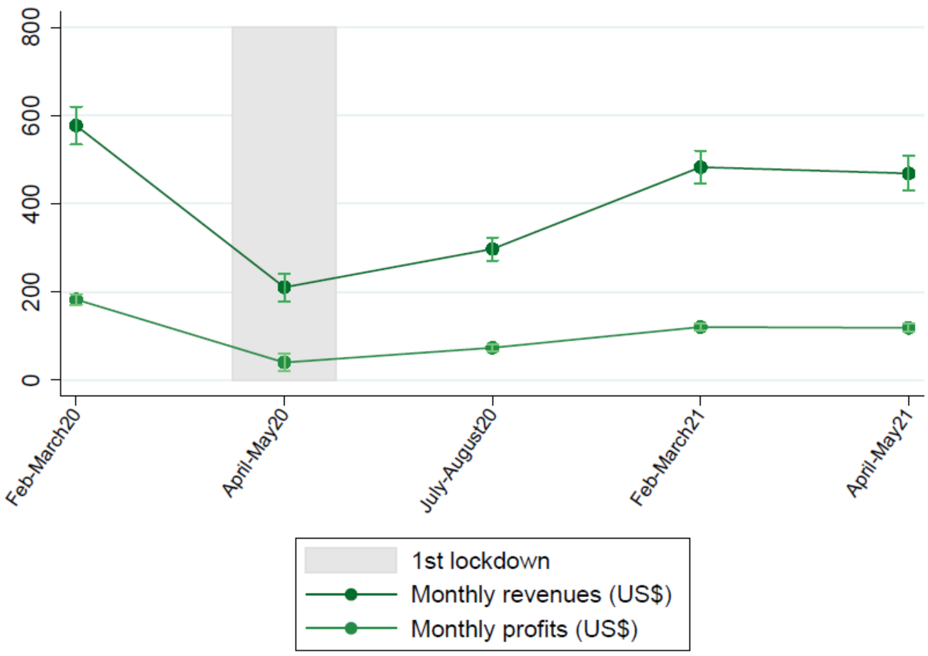


2. Revenues and profits are still lower one year after the onset of the pandemic.

At Figure 2 shows monthly revenues and profits between February 2020 and May 2021. Even for firms that managed to stay open, both revenues and profits suffered a significant drop during the first lockdown. With respect to pre-lockdown levels, revenues decreased by 48.5% and profits by 60% in the months immediately after the lockdown was lifted (July-August 2020).

One year after the onset of the crisis, revenues were still 19% lower and profits 36% lower than their pre-lockdown levels. Thus, although most businesses reopened, firm owners suffered sizeable income losses. This shows that the lockdown had persistent effects on firm performance and the recovery has been slow.

Figure 2: Average monthly revenues and profits



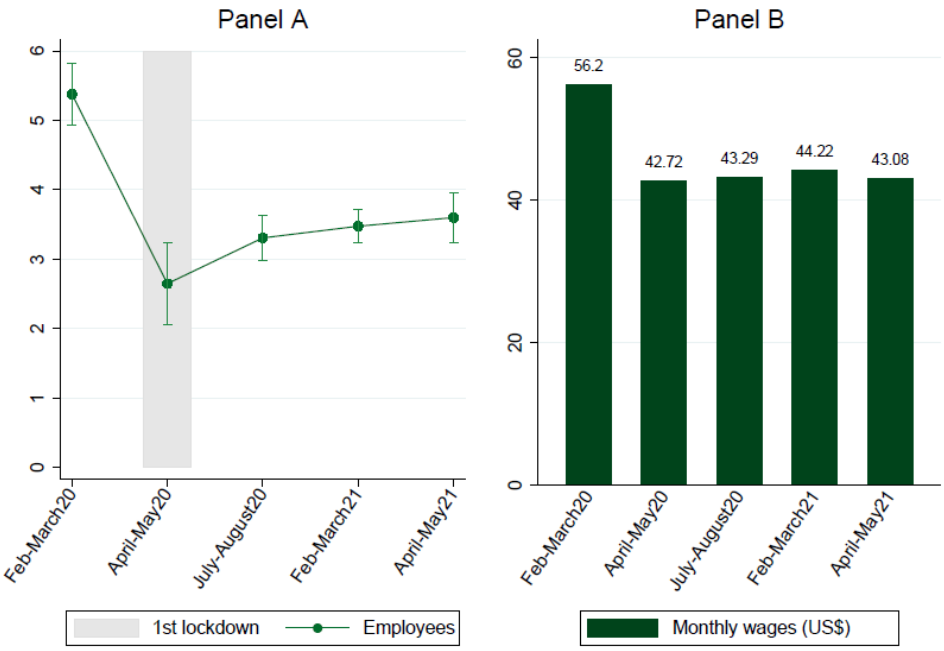
3. Employment and wages also suffered.

The general trend in the number of employees follows the one described above for revenues and profits, with a substantial drop during the first lockdown and a partial recovery in the following year.

Panel A of **Error! Reference source not found.** shows the average number of employees across the different periods: in July-August 2020, operating firms had on average 61% of the employees relative to the pre-lockdown period. Employment hardly recovered as the crisis evolved: in April-May 2021, firms only employed around 66% of their pre-lockdown workforce. This is despite a drop in wages by 24% (Panel B), suggesting that firms had to resort to workers' layoffs to deal with the sizeable decrease in revenues. The effects of COVID-19 on firms were therefore passed on to workers as well, translating into lower employment and wages.

We also find that firms tried to decrease labour costs by hiring less skilled and cheaper workers: new employees hired between January and May 2021 were mostly unskilled (40% had no experience nor a VTI degree), while 79% of workers who were fired since the beginning of the crisis had substantial experience within the firm.

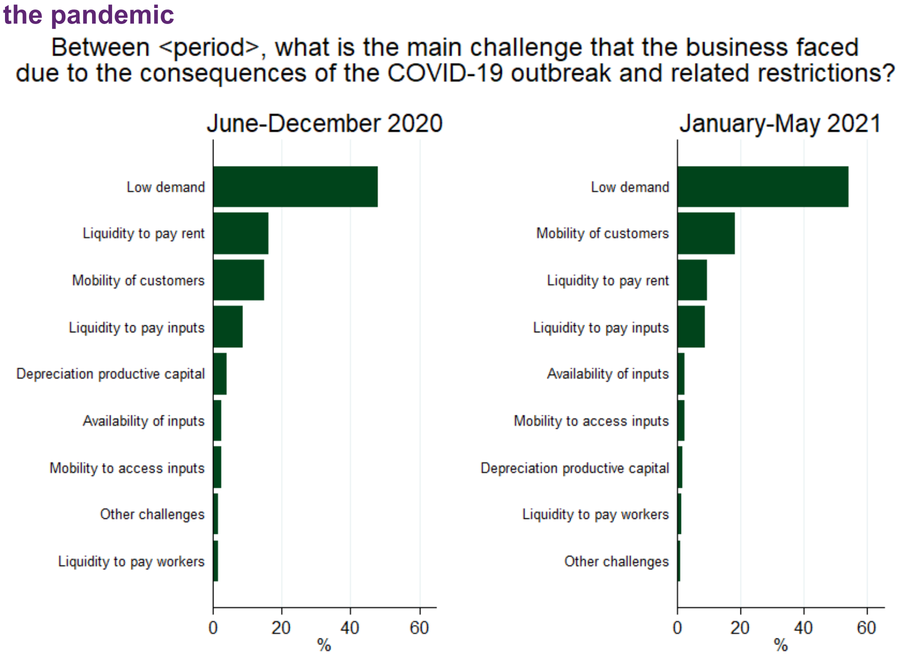
Figure 3: Average number of employees (Panel A) and monthly wages (Panel B)



4. Low demand and lack of liquidity as key challenges reported by firm owners.

To better understand the drivers behind these trends in performance, we asked firm owners to identify the main challenges they faced in the 6 months preceding each survey. We report their answers in Figure 4: low demand – either because of customers' lack of income or difficulties in mobility – and subsequent lack of liquidity to pay rent and inputs are the key challenges indicated at both points in time.

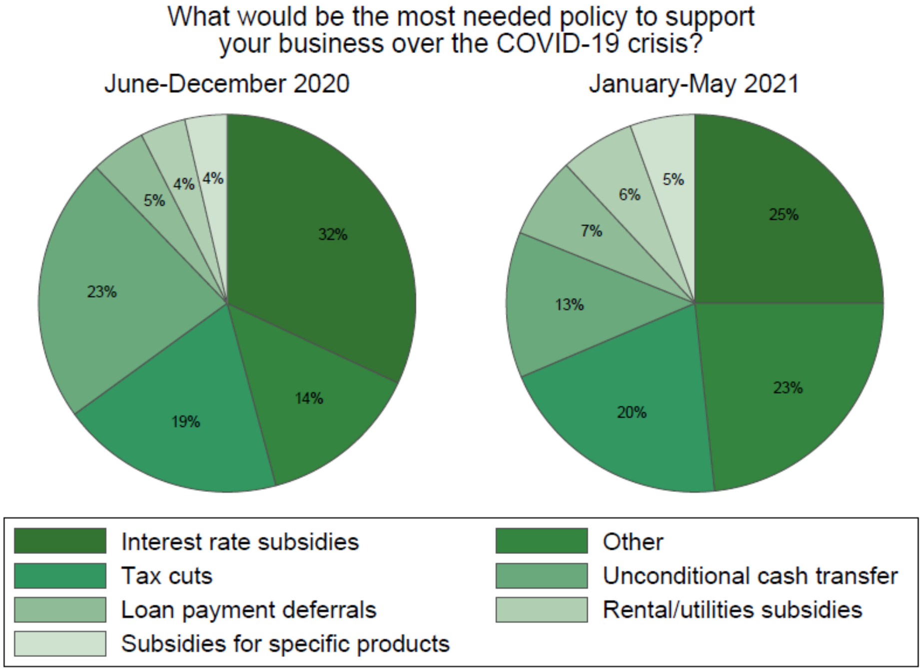
Figure 4: Low demand has consistently been the main challenge related to the pandemic



5. Firms’ demands for policy support reflect their need for liquidity

When asked which is the most needed policy for their business, more than half of the owners replies interest rate subsidies, tax cuts, and unconditional cash transfers (Figure 5). This has not changed much since the onset of the crisis.

Figure 5: The need for liquidity



Policy implications

Our results are important for designing programs that encourage the recovery from the large economic shock caused by the pandemic.

Our findings suggest that while permanent firm closures were limited, the recovery has been slow: one year after the pandemic started, demand is still low, and profits, wages as well as employment are substantially below pre-pandemic levels. At the same time, firm owners are experiencing significant difficulties in meeting their liquidity needs to keep firms open.

These results suggest two main directions for policy intervention.

1. First, policy actions that can boost the spending power and ease the mobility of customers will be important to make sure that demand is sustained during the recovery period.

2. Second, policies that can facilitate liquidity access for firms – such as interest rate subsidies, tax cuts/deferrals, and unconditional cash transfers – will be critical to ensure that firms can remain open and keep paying their employees in the path to recovery.

References

Alfonsi, L., Bandiera, O., Bassi, V., Burgess, R., Rasul, I., Sulaiman, M., and A. Vitali, (2020). Tackling Youth Unemployment: Evidence from a Labor Market Experiment in Uganda, *Econometrica*, 88(6), 2369-2414.