Export promotion and import substitution: Opportunities (and threats) from the COVID-19 shock?

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Covid-19 disruptions caused a 43% reduction in imports

Source: BoU, 2020
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Two possible responses to this...

• An opportunity
  • *Since the pandemic (...) started taking its toll on the economy, the phrase ‘import substitution’ has become a buzzword.* (Daily Monitor 2020)

• A threat
  • “Manufacturing: has declined on account of disruptions to the inflow of raw materials" and "(...) products that we import from China (...) have increased in price and reduced in supply" (Presidents Investor's Roundtable, 2020).

• NDP III: “Export promotion and import replacement will be strategies to ensure production for domestic, regional and international markets.”
Why we should take the threat seriously

• Impact on intermediaries

• Impact on employment

• Impact on productivity
COVID-19 had no impact on consumption goods

Source: Rauschendorfer and Spray, 2020
Covid-19’s led to sizeable reductions in intermediary and capital goods

Source: Rauschendorfer and Spray, 2020
Examples of intermediary goods hit include iron products, medicines, and packaging.

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Source: Rauschendorfer and Spray, 2020
Many supply chains rely on imports

Two factories (blue), rely on imports (black) from 96 foreign suppliers from 28 different countries

Source: Carvalho, Elliott and Spray, 2020
Simulations of a reduction in imports cause large reductions in firms and employment

- Reduction in imports in line with COVID-19 shock
  - 6.6% reduction in active firms and 4.7% reduction in formal employment

- It will disproportionately impact firms in important sectors
  - Manufacturing sectors
  - Tea and coffee production
  - Hospital sector
  - Transport sector
Why we should take the threat seriously

• Impact on intermediaries
  • Reduce intermediary inputs essential for Ugandan production

• Impact on employment
  • Will hurt employment as some firms rely directly or indirectly on imports

• Impact on productivity
  • Will hurt key sectors – medical, building materials, manufacturing
Is there an opportunity?

- Yes, if targeted **competitive** domestic production
  - Chance for firms to reevaluate supply-chain decisions – supplier development
  - Policies to encourage **globally competitive** production of medical supplies – masks, gloves, etc.

- Only then can achieve goals of NDP III: “increase the product range and scale for import substitution and improved terms of trade....Key expected results include: increased share of manufactured exports in total exports, growth in the industrial sector contribution to GDP, and increased share of labour force employed in the industrial sector”

- However, mandating local sourcing may be counter-productive
  - May lower productivity which in the LR harms firms
  - May harm consumers
Where to focus? Top 20 Anchor firms

• Manufacturing firms
  • Building materials, food processing, etc.

• Service industries
  • Financial services, packaging, telecoms, etc.

• Utilities sectors
  • Electricity, water, etc.
Policy Recommendations

• Supplier development programmes in an age of COVID
  • Facilitate digital matchmaking platforms and invest in joint programmes with large firms to subsidise capacity building.
  • NDP III: “Government will scale up interventions to increase use of locally procured goods and services through use of preference schemes and investment in supplier development programmes.”
  • Budget recommendation: Budget to be allocated to UIA for local content programme where large FDI firms are provided funding to work with local suppliers on product development, training, quality control.

• Eliminate tariffs on crucial imported inputs
  • I.e. inputs that are needed for competitive production to boost import substitution and exports of final, high-value products.
  • NDP III: “Increased share of intermediate goods (inputs for manufacturing) in total import bill from 18 percent to 25.5 percent.”
  • Budget recommendation: MoFPED to set up a task force on tariff policy and conduct quarterly workshops with the private sector to review the tariff schedule for the upcoming fiscal year.

• Trade facilitation
  • Strengthen electronic infrastructure that minimizes human contact and reduces the cost of trading (e.g. Uganda Electronic Single Window).
  • NDP III: “… strengthening electronic systems in submission of export and import documentation.”
  • Budget recommendation: Assign a budget to the URA dedicated to improving electronic trade facilitation in Uganda (e.g. institutions to move their services to the UESW through dedicated workshops with technical personnel).