EPRC ECONOMIC POLICY RESEARCH CENTRE

POLICY NOTE

Policy Note: 10, *March 2022*

What explains Uganda's surge in laundry soap and cooking oil prices in 2021/22?

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Executive Summary

This policy note investigates the recent spike in laundry soap and cooking oil prices in Uganda between June 2021 and March 2022. The upsurge primarily explained the price increase in the price of Crude Palm Oil (CPO) —the key raw material for making soap and cooking oil. Evidence reveals that between July 2021 and February 2022, the contribution of the international price of CPO in the final retail price drastically increased to 63 percent from 57 percent registered in the first half of 2021 (January to June 2021). Imposing of an import duty on CPO in July 2021 also affected the input mix used by manufacturers. To a lesser extent, the gradual rise in international shipping costs and the increase in global fuel prices also contributed to the escalation of soap and cooking oil prices. The study recommends a temporary waiver of the 10 percent import duty and 1.5 percent infrastructure levy on CPO and related product imports to contain the recent surge in commodity prices in the short term. Implementing this measure could increase the importation of CPO and stabilise the prices of laundry soap and cooking oil by lowering the raw material cost for soap making.

1.0 Background

Laundry soap and cooking oil are vital daily consumption commodities for most urban and rural households in Uganda.The household consumption of soap and cooking oil is directly linked with Sustainable Development Goals (SDGs) 6 and 2, respectively. Accordingly, target 6.1 aims to achieve access to adequate and equitable sanitation and hygiene for all and end open defecation, paying particular attention to the needs of women and girls and those in vulnerable situations. Moreover, indicator 6.2.1 monitors the proportion of the population using safely managed sanitation services, including a hand-washing facility with soap and water. On the other hand, SGD 2, target 2.2 aims to end all forms of malnutrition and wasting in children under 5 years of age and address the nutritional needs of adolescent girls, pregnant and lactating women and older persons. Besides general sanitation, the washing of hands with soap and water is one of the Standard Operating Procedures (SOPs) put forward by the World Health Organisation (WHO) to contain the spread of the coronavirus disease (COVID-19). Examining the drivers of the recent escalation of prices for both commodities is worthy of policy attention to ensure citizens' welfare.

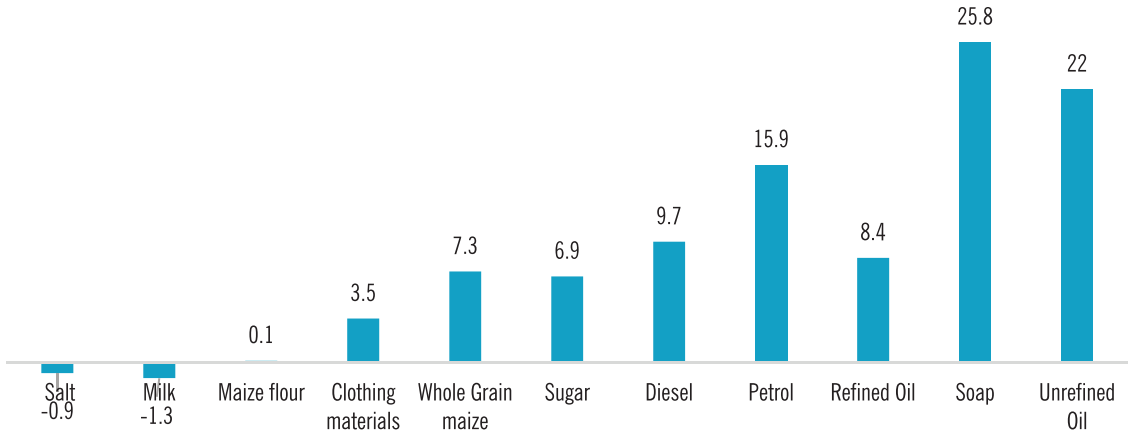
2.0 Why is the drastic price increase of concern for policy makers?

Over the last three (3) months, the price of several essential commodities and services in Uganda has increased tremendously (Figure 1). For example, between December 2021 and February 2022, the price of a bar of laundry soap increased by about 26 percent. Other significant increases in prices were registered for cooking oil (refined or unrefined), petrol (16%), and sugar (10%)—only salt and milk registered declines in prices over the same period.[1]

Notably, the retail prices of laundry soap and cooking oil have escalated faster than the prices for most commodities, especially between January and February 2022. During this period, the national average retail price for laundry bar soap rose by 22 percent, from UGX 4,257 in January to UGX 5,213 per kg in February 2022. Except for sugar, the other essential commodities mainly depend on imported inputs—whose prices have increased drastically since July 2021 due to international and domestic factors. Therefore, the enormous magnitude of the recent price spikes for essential household commodities over a relatively short period could negatively affect the cost of living and general welfare, political stability and malnutrition. More importantly, it could also reverse Uganda's gains towards SDGs 6 and 2.

1 This policy note does not focus on changes in petrol prices—these were examined in detail by Odonkoyero and Bulime (2022).

Figure 1 Changes in the consumer price index for selected commodities, December 2021- February 2022 (%)



Source: Authors' construction using the Uganda Bureau of Statistics (2022) – February CPI Release.

The explanations of the recent surge in commodity prices by the Government, the general public and the media are primarily anecdotal, without a thorough diagnosis of the critical drivers – both domestic and international. Notably, there is limited evidence on the proportion of the price increase attributed to several plausible factors such as taxes and the CPO price. Second, price increases undermine poverty reduction efforts because they increase the cost of living as they are transmitted to household expenditure budgets and consequently affect food consumption patterns for the poor. UBoS (2021) shows that the poor spend disproportionately a higher share of their total household expenditures (over 40%) on food. There has been limited analysis on how global commodity prices translate into domestic retail prices.

Therefore, this policy note aims to generate evidence on the cost drivers of the recent escalation of the retail price for laundry soap and cooking oil in Uganda. These two commodities are prioritised because they experienced higher price increments than other commodities, as shown in Figure 1. It is envisaged that the results can offer workable policy actions in the short and medium-term to curb the runaway laundry soap and cooking oil prices.

3.0 Objectives of the study

Specifically, this policy note answers the following research questions.

(a) What have been the trends in domestic retail prices for laundry bar soap and cooking oil over the past two years, focusing particularly on 2020 and 2021?
(b) What are the key drivers of the recent surge in domestic retail prices of laundry bar soap and cooking oil?
(c) What short-term policy measures should be implemented to halt the price escalation of cooking oil and laundry bar soap.

The rest of the paper is structured as follows. Section 4 discusses the methods and data sources used in the analysis. Section 5 discusses the trends in domestic retail price movements, while section 6 delves into the potential drivers of the recent surge in retail commodity prices – findings of the decomposition analysis and international price transmission mechanisms. The conclusion and potential corrective policy measures are presented in section 7.

4.0 Methods and data sources

To achieve the objectives of the study, qualitative and quantitative methods were utilised.

4.1 Qualitative methods

Desk reviews

To examine the causes of the recent increase in the prices of select commodities, the study relied on the review of existing literature and policy documents, including the Uganda Revenue Authority Tax amendment report 2021/2022, the National Budget speech 2021/22, Consumer Price Index reports and Producer Price Index report by Uganda Bureau of Statistics (UBoS), among others. The desk reviews highlighted the recent developments in the Crude Palm Oil (CPO) industry, including but not limited to tax policy changes, export restrictions on CPO, production and export trends, supply side constraints, and global geopolitical tensions that affect the international movement of commodities.

Key Informant Interviews

Key Informant Interviews (KIIs) were used to triangulate the findings from the quantitative data sources and develop an understanding of the recent changes in both the domestic and international business environment, the study conducted key informant interviews (KIIs) with Uganda's leading laundry soap and cooking oil manufacturers. The KIIs enabled in-depth discussions of the quantitative results obtained from quantitative data analysis.

4.2 Quantitative methods

Secondary Data

The data used in this study were obtained from both domestic and international sources. Data on the retail prices of laundry bar soap and cooking oil, producer price index and consumer price index were obtained from the Uganda Bureau of Statistics. Data on imports (volumes, value and revenues) of CPO and close substitutes (Palm Stearin and Palm Olein) were obtained from Uganda Revenue Authority. International prices of CPO, crude palm Olein, refined palm stearin and palm fatty acid distillate were obtained from the World Bank Commodity Market database and Reuters. The production volumes of Malaysian CPO were obtained from the Malaysian Palm Oil Board website.

4.3 Analytical Approach

This policy note triangulated the findings from the literature survey together with KIIs and the secondary data. The quantitative estimations entailed descriptive analysis. Three analytical methods were employed.

(a) Trend analysis of the average retail prices for both cooking oil and laundry bar soap and international prices of CPO was undertaken.

(b) A decomposition analysis of the retail prices of laundry bar soap and cooking oil was undertaken. Here the final costs for laundry bar soap and cooking oil were broken down into their components to determine which part explains the most extensive variation in the final retail price.

(c) Lastly, the pass-through coefficients were computed to measure how international Crude Palm Oil prices are passed on to the final retail price of cooking oil and laundry bar soap. Equation 1 shows the computation of the pass-through coefficient. It is a ratio of the change in retail prices for laundry bar soap and cooking oil to changes in the international CPO price. The pass-through coefficient is interpreted as the transmitted effect of a unit dollar increase in international CPO price to the domestic retail price of cooking oil and laundry bar soap.

$$(1) \quad PT_{it} = \frac{Retail\ price_{i,t} - Retail\ price_{i,t-1}}{CPO\ price_{i,t} - CPO\ price_{i,t-1}}$$

Where *PT* is the pass-through coefficient for i^{th} country (Uganda) at t^{th} time (month/year). The *retail price* is the domestic retail price for cooking oil and laundry bar soap, and the *CPO price* is the international CPO price.

Note: To undertake the decomposition and the transmission mechanism analysis, all local prices were converted into United States Dollars (USD) using the average exchange rate for a given period. We got the average of both commodity prices to make the computation tractable. At the time of this study, we could not accurately disaggregate the individual share of cooking oil and laundry bar soap in the litre or price of CPO. Both cooking oil and laundry soap are obtained from refining CPO.

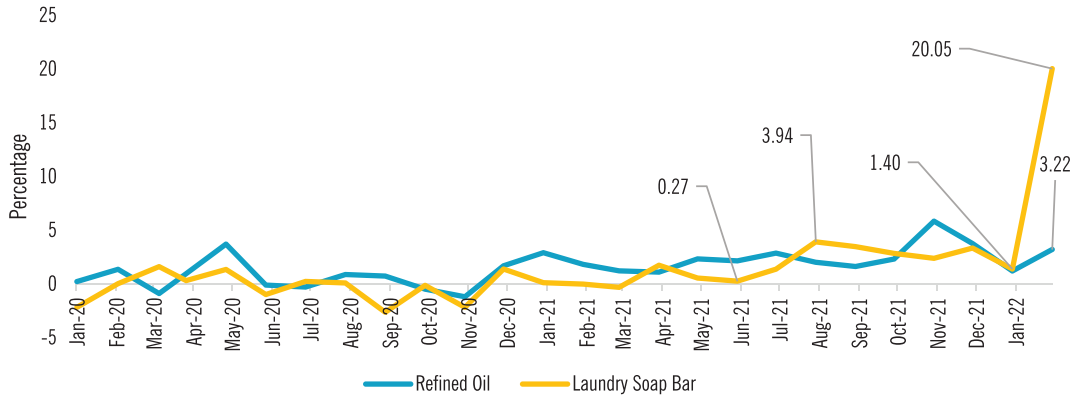
5. How have laundry soap and cooking oil prices evolved?

Before examining the cost drivers for the recent escalation of retail prices, the study examined the trends in the retail price of cooking oil and laundry soap to establish whether the price spike exists, its duration and how retail prices have evolved.

5.1 Changes in the consumer price index (CPI)

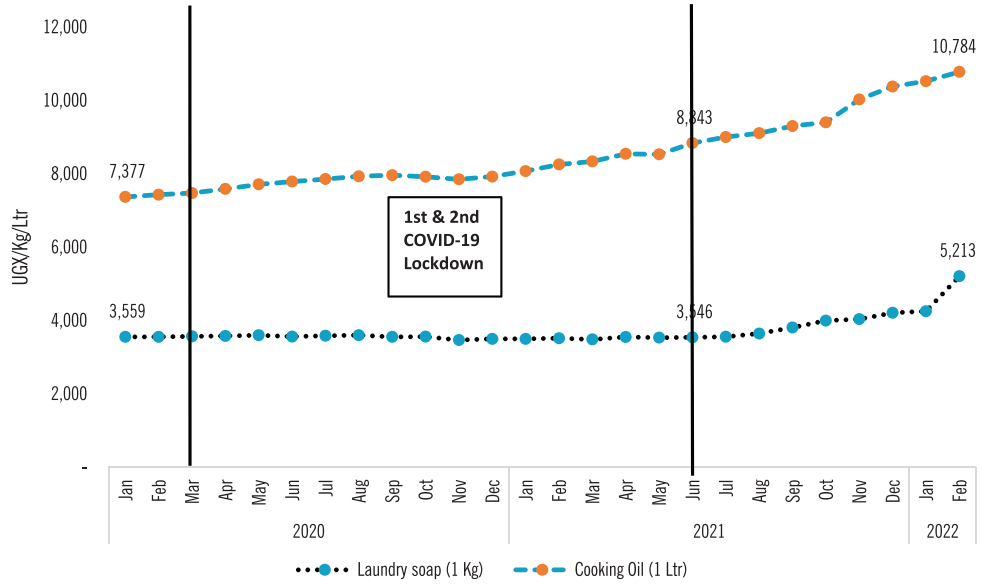
Figure 2 shows that the monthly change in refined cooking oil and laundry soap price fluctuated steadily between June 2021 and February 2022. Laundry soap prices were more volatile than refined cooking oil prices. This fluctuation partly reflects the differences in the (i) relative importance of the two products to consumers -unlike cooking oil that is used only for cooking, laundry soap in Uganda is used for washing clothes; utensils; bathing and cleaning the house, among others (ii) lack of close substitutes -unlike soap, the

Figure 2 Monthly change in CPI for refined oil and laundry soap % (January 2020 – February 2022)



Source: Authors' construct using data from UBOS (2022)

Figure 3 Trends in the retail price for laundry soap and cooking oil (January 2020 – February 2022)



Source: Authors' construct using data from UBOS (2022)

consumption of cooking oil can be done away with on health grounds or entirely halted by households in case of a price spike. Notable changes in the CPI for laundry soap are observed between January 2022 and February 2022, i.e. the CPI increased by about 20 percent.

5.2 Trends and patterns in the final retail commodity price

The retail prices for laundry soap and cooking oil were relatively stable until June 2021 (Figure 3). After July 2021, the prices of these two commodities escalated.

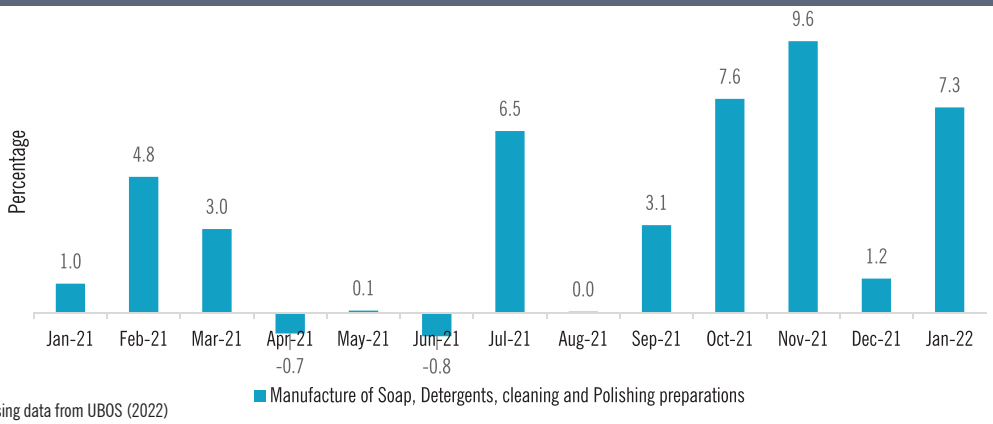
Besides, the July 2021 tax amendments key informant interviews with soap manufacturers revealed that the investments for compliance with the digital tax stamps have also been factored into the final prices of these commodities. Specifically, a soap manufacturer stated that;

"Our company invested between USD 1-2 million to install and facilitate the operation of the recently introduced Digital tax stamps. The investment cost was all borne by the manufacturers. Currently, each digital tax stamp costs us around UGX 40 per packet that we produce. We factor this cost into the final selling price of these commodities. If the Government wants to improve its tax collection efficiency, it should be ready to invest partly into it." (KII, Thursday, March 3rd 2022).

5.3 Trends in the Producers Price Index (PPI)

Besides examining how the general consumer prices (CPI) changed, the prices received by manufacturers for their goods and products (PPI) were reviewed to find out the change in the costs of the two commodities. Figure 4 shows a drastic upward change in soap manufacturers' prices in December 2021 and January 2022.

Figure 4 Percentage change in PPI for soap, detergents cleaning and polishing preparations (January 2021 – February 2022)



Source: Authors' construct using data from UBOS (2022)

Specifically, manufacturers of soap, detergents, cleaning and polishing preparations recorded an increase of 7.3 percent in their selling prices in January 2022, up from 1.2 percent in December 2021. This evidence further reveals that the monthly inflation for manufactured soap, detergents, cleaning and polishing preparations has been increasing over the past seven months starting July 2021 – partly reflecting an increase in the cost of living.

6.0 What explains the recent upsurge in laundry soap and cooking oil prices?

The findings in this section are based on desk review, key informant interviews and secondary data analysis. Overall, the recent upsurge in the retail prices of laundry soap and cooking oil is mainly driven by the following factors: (i) the recent upsurge in the international price of CPO and other critical raw materials for making laundry soap and cooking oil, (ii) imposition of import duty on CPO; (iii) increase in shipping costs; and (iv) increases in the domestic and international price of fuel.

6.1 Recent upsurge in the cost of raw materials

(i) Palm oil

Palm oil[2] is the primary raw material for manufacturing cooking oil and laundry soap. In Uganda, most cooking oil and laundry soap manufacturers import CPO from Malaysia and Indonesia at the internationally set commodity prices at the world's principal commodity exchanges.[3] Figure 5 shows that global CPO prices started increasing, albeit steadily, from May 2020, until April 2021, when prices gradually subsided. However, the price slump between April and May 2021 was not sustained as global CPO prices increased steadily until December 2021. International CPO prices suddenly spiked between December 2021 and March 2022. For instance, the price of CPO increased by 41 percent (i.e. USD 555 per metric tonne) from USD 1,345 in January 2022 to USD 1,900 in March 2022.

The recent spike in the international palm oil price observed between January and March 2022 is explained by various factors. *First,* the increased demand for palm oil, driven by the growing CPO importation by China and India[4] following the full re-opening of the economy after the COVID-19 restrictions; the decrease in the global soybean oil exports from Brazil, Peru, Argentina because of prolonged dry weather; and the reduced Sunflower oil exports from Russia and Ukraine- the two largest exporters of sunflower oil, because of the outbreak of war in February 2022. The reduction in the supply of these close substitutes of CPO has increased its global demand and propped up the prices of palm oil and related products. Jadhav (2022) reported that increased near month purchases of CPO (between February and March) by Asian (especially India) and European palm oil refiners to secure replacements for sunflower oil shipments because of the ongoing Ukraine-Russia war.[5] The ongoing Ukraine-Russia war has also fuelled speculation by futures traders in commodities such as palm oil, edible oils and oilseeds. This speculation will likely result in further price spikes in crude palm oil prices in the coming months.

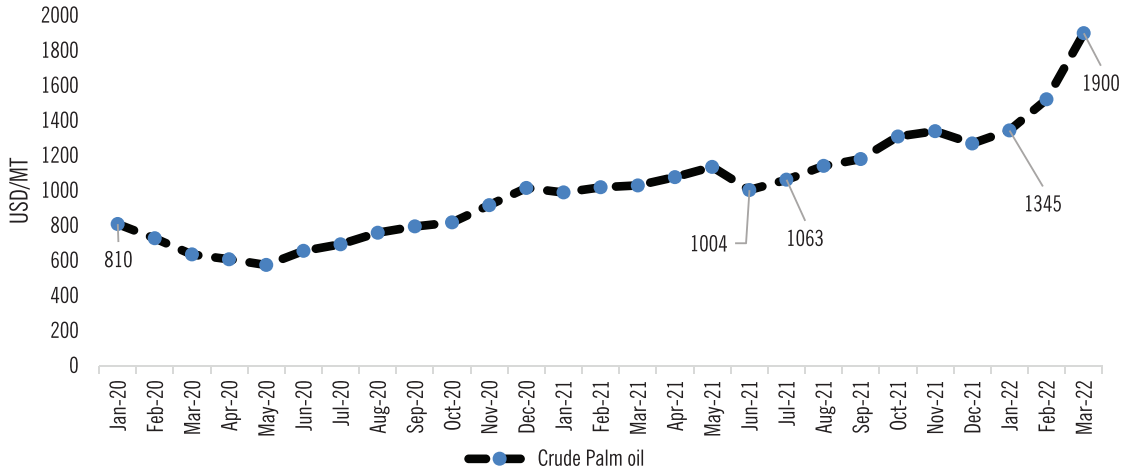
2 Palm oil (including its fractions) is traditionally used for edible purposes such as cooking and frying, in addition to being a choice ingredient of food formulations (e.g. shortenings and confectionery).

3 Indonesia (59%) and Malaysia (25%) were the world's leading exporters of crude palm oil in 2021, that is about 84 percent of the global export market share (USDA, 2022).

4 The two largest buyers of palm oil globally. In 2022, China's palm oil consumption is expected to increase due to a lower supply of rapeseed oil and soybean oil. China is also seen to buy more palm products for its animal feed. In 2022, India's palm oil purchase is likely to be spurred by recovery in its hotel, restaurant and catering segment and its government's lowering palm oil import duties (CPOPC, 2022).

5 Ukraine and Russia are the world's leading exporters, collectively accounting for 75 percent of the global export supply of sunflower oil.

Figure 5 Monthly global price trends for Crude Palm oil



Source: Author's computation based on World Bank Commodity Markets database (2022). Accessed at https://www.worldbank.org/en/research/commodity-markets

Second, in February 2022, Indonesia further caused global supply disruptions of CPO, resulting from export restrictions such as charging a higher tax on CPO exports (USD 200 per metric tonne) and requiring all exporters to obtain export permits for all palm oil products. The tax on palm oil export aimed to support the expansion of Indonesia's palm biodiesel program to use more palm oil for blending transport fuels to cut energy imports. Further, to obtain export permits, companies must sell 20 percent of their planned exports to the domestic market at a capped price. Major CPO exporters adopted this measure to curb the rising domestic cooking oil prices.

Third, the decline in CPO production volumes and exports for Malaysia and Indonesia over the past months. For example, Malaysia's production volumes reduced by 26.7 percent from 1,710,356 tons in August 2021 to 1,137,448 in February 2022, and the trend is likely to continue (Figure 6). The current decline in production for Malaysia is because of heavy rainfall, increasing fertiliser costs, flooding, and labour shortages[6] (CPOPC, 2022). On the other hand, the decline in Indonesia's exports is due to new export restrictions and the low application of fertilisers. Generally, both countries have also reported a slowdown in the new plantings of palm oil trees.

Therefore, since Uganda is a net importer of CPO and related products, the increase in international palm oil prices affects the manufacturer's cost of production through a price transmission effect to the price of manufactured commodities such as laundry soap and refined oil hence increasing the domestic retail prices.

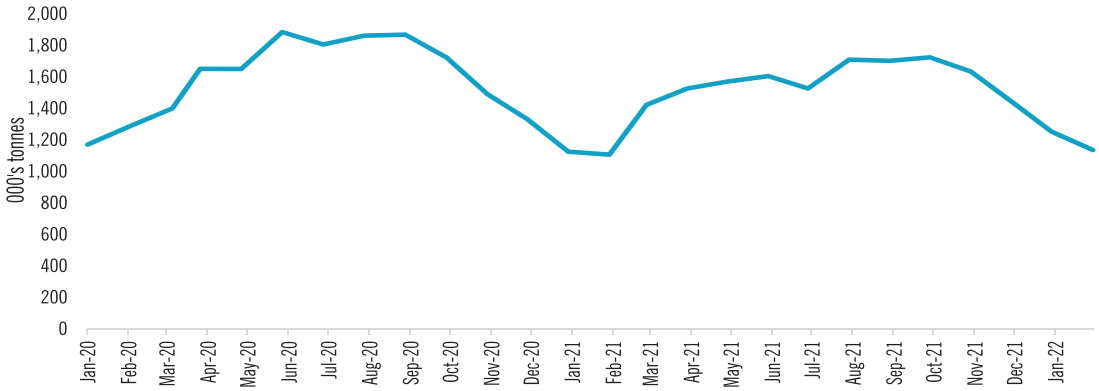
(ii) Increase in price of substitute raw materials

Besides CPO, laundry soap and cooking oil can be manufactured by refining cheaper and alternative semi-processed by-products of CPO, namely, Crude Palm Olein (COL), Refined Palm Stearin (RPS) and Palm Fatty Acid Distillate (PFAD). However, the global price trend of these substitutes follows a similar pattern as that of the CPO prices (Figure 7).

This is not surprising since all three substitutes are obtained by refining CPO. Hence it is probable that their prices are determined by the prevailing global price of the CPO. Figure 7 also highlights

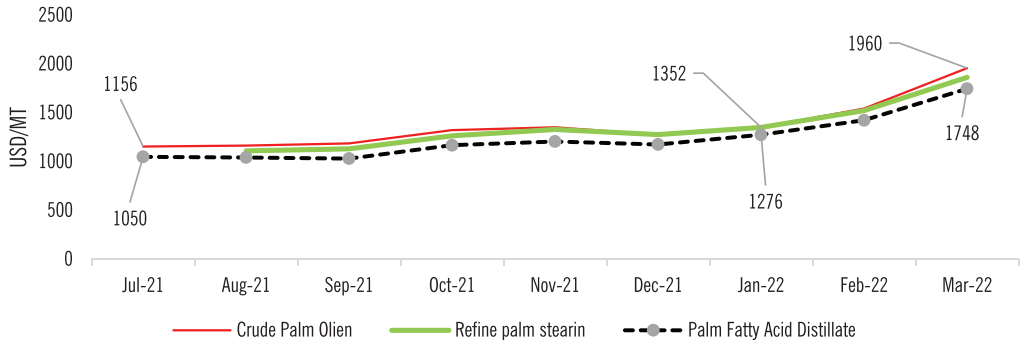
6 The COVID-19 induced border closures reduced the supply of foreign workers in the country's oil palm estates who had returned to their home countries.

Figure 6 Malaysia's production of crude palm oil (January 2020 – January 2022)



Source: Authors' construct using data from Malaysian Palm Oil Board (2022)

Figure 7 Monthly price trends for Crude Palm Olein, Refined Palm Stearin and Palm Fatty Acid Distillate



Source: Authors' computation based on Daily Reuters Commodity exchange data (2022).

that while the international prices of these CPO by-products recently spiked, they remained relatively lower than those of CPO (Figure 5). Local soap manufacturers prefer CPO to these by-products for several reasons. First, CPO yields a higher content of soap stock (Fat) after refining than its by-products (Crude Palm Olein, Refined Palm Stearin and Palm Fatty Acid Distillate). This implies more soap making material for soap manufacturers. These findings corroborate with information from a critical informant interview (KII) with a soap manufacturer,

"When we process CPO, we get 70 percent cooking oil, 29 percent fat (soap stock) and 1 percent palm fatty acid distillate. However, we produce 80 percent cooking oil, 19 percent fat (soap stock), and 1% palm fatty acid distillate with palm oil fractions. Therefore, we get less fat for making soap by shifting from CPO to palm oil fractions. To circumvent the high CPO prices, we have had to increase our relatively less costly palm oil fractions imports. However, these are also subject to a 10 percent import duty and 1.5 percent infrastructure levy." (KII, Thursday, March 3rd 2022).

Second, a majority of the laundry soap and cooking oil manufacturers in Uganda heavily invested in refineries, which require high maintenance costs. These refineries are suitable for CPO and not semi-processed CPO by-products. Therefore, most manufacturers continue to import highly-priced CPO so that their machines are not redundant. Indeed, an interview with a soap manufacturer revealed that,

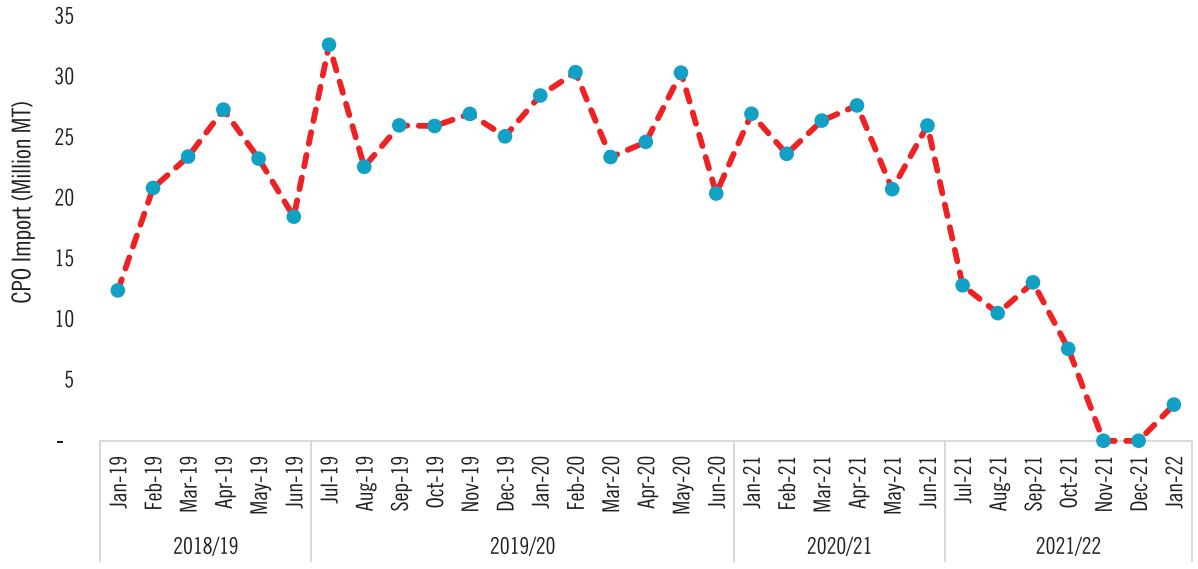
"We have invested approximately USD 10 million to establish our refinery, which we also use to refine locally produced sunflower into sunflower oil for export to Europe. However, the refinery capacity is underutilised due to low domestic sunflower production. We buy sunflower seeds from South Africa, sell them to local farmers, and recruit and facilitate agricultural extension workers with motorcycles and laptops. Some of these costs should have been borne by the government" (KII, Thursday, March 3rd 2022).

6.2 Imposition of taxes on crude palm oil imports.

Through the national budget, the Government undertook custom amendments and introduced a 10 percent import duty on partly refined base oil (URA, 2021). This import duty attracts a 1.5 percent infrastructure levy. Figure 3, section 5.2 above, shows domestic retail prices for laundry soap and cooking oil increased after Government adopting a uniform tax regime for all crude palm oil-related products.

Before July 2021, the importation of CPO was zero-rated while its fractions (i.e. Palm oil stearin, Olein and Palm Fatty Acid Distillate) attracted a 10 percent import duty. This gap created room for smuggling emanating from the misdeclaration of the two related products. Indeed, Figure 8 reveals that with imposing the new taxes, import volumes of CPO, the critical raw material for laundry soap and cooking oil manufacturing, drastically declined from 26 million tonnes to about 1,280 tonnes in November 2021.

Figure 8 Trends in Crude Palm Oil imports, volumes (January 2019- January 2022)



Source: Author's computation based on data from Uganda Revenue Authority (2022)

Although import volumes have rebounded, this has been at a much slower pace than before June 2021. While it is plausible to conclude that imposition of an import duty resulted in a slump in CPO imports for Ugandan soap manufacturers, this decline also coincided with a drastic increase in the CPO price in the international market (see section 6.1, Figure 5). Indeed, between July 2021 and February 2022, the international CPO price increased by 43.2 percent. This, in turn, drastically reduced the total CPO import tax revenue collected by Government (See Figure A1, Annex).

The rapid escalation of CPO prices amidst an unfavourable tax environment led most manufacturers to substitute CPO with its cheaper palm oil fractions — Palm Stearin and Olein. Indeed evidence in Figure 9 reveals that starting from July 2021, soap manufacturers drastically increased the importation of Palm Stearin relative to Palm Olein.[7] This is because Palm Stearin is cheaper than CPO in the global market, although it produces less fat content for soap manufacturing. However, the growth in palm stearin imports was short-lived as imports slumped by 61 percent between November 2021 and January 2022. Besides producing a lower fat content for soap making than CPO after refining, palm stearin is also subject to a 10 percent import duty. Therefore, by January 2022, the decline in the import volumes of all soap and cooking oil-making raw materials affected retail prices.

7 Palm stearin is the harder fraction of Palm oil, contains a higher fraction of saturated fatty acids and is mainly used as natural hard stock for soap making. On the other hand, Palm Olein is the liquid fraction of Palm Oil and suitable as cooking oil for blending with Soya bean oil, corn oil or canola oil.

Figure 9 Trends in Palm Stearin imports, volumes (January 2019 - January 2022)

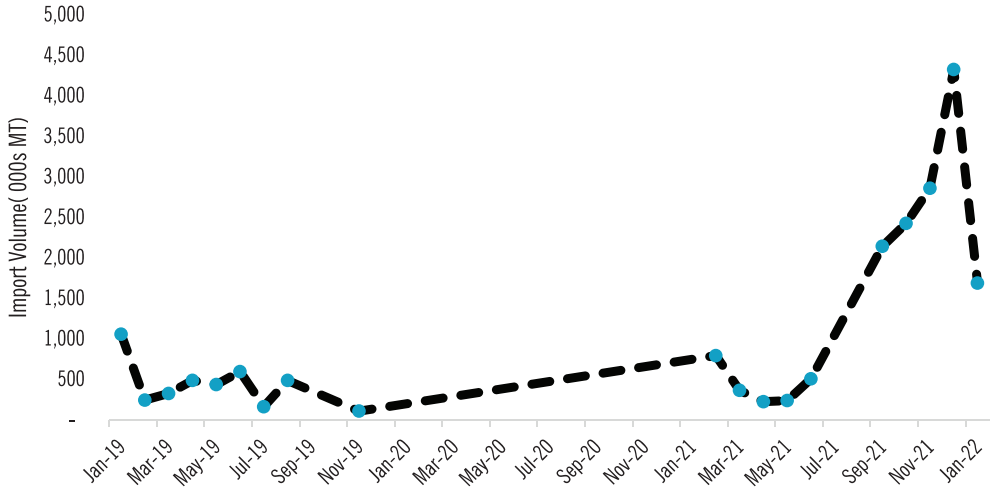
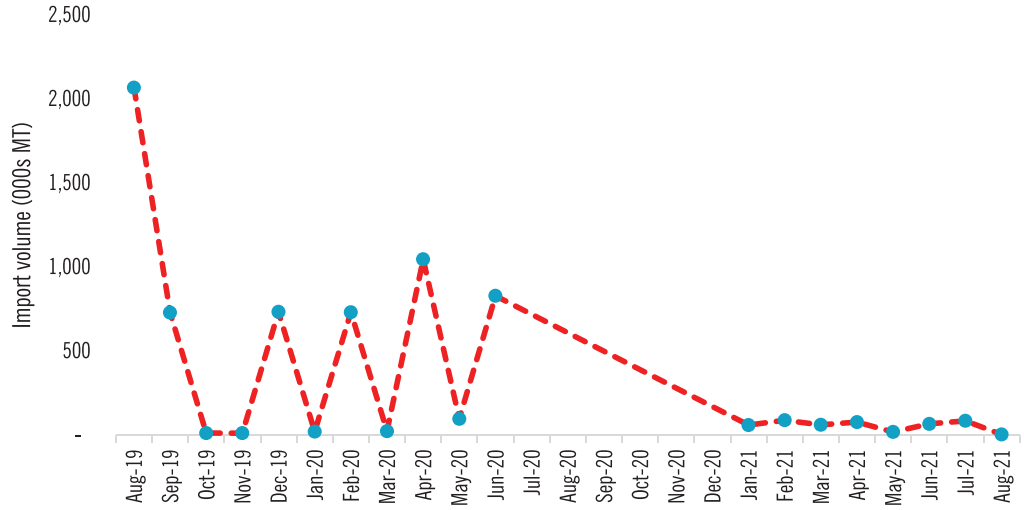


Figure 10 Trends in Palm Olein imports, volumes (January 2019- January 2022)



Source: Author's computation based on data from Uganda Revenue Authority (2022)

Soap manufacturers corroborated the above evidence as illustrated ;

> *"Currently, the domestic supply of raw materials stands at about 10 percent while the consumption demand for these products is approximately 90 percent. Although well-intentioned to boost local value addition, imposition of excise duty widened the deficits in raw material supply and was transferred to the final retail price." (KII, Friday, March 4th, 2022).*

Another manufacturer stated as below;

> *"We currently access only 4000MT of CPO from refining palm oil fruits produced domestically. However, to satisfy the domestic demand, our refinery requires between 10,000 and 12,000 metric tons of CPO. We import the rest." (KII, Friday, March 4th, 2022).*

Although imposing the 10 percent import duty on CPO was undesirable to most soap and cooking oil manufacturers, the amendment could have prevented potential smuggling characterised by the importation of palm oil fractions and declaring them as CPO, which was zero-rated, up to June 2021. Indeed, evidence (Annex, Table A1) suggests that introducing the import duty in July 2021 could have increased the total tax collection. Table 1, which estimates the costs of producing cooking oil, partly shows that the tax changes cannot explain the recent surge in prices.

5.3 The gradual surge in the international transport cost.

The COVID-19 pandemic is also associated with supply chain disruptions, delays in delivering raw materials, increasing demand for ocean freight transporting CPO and related products and the reduced capacity to meet growing demand in the freight markets. This increased the transportation costs – especially shipping costs. For instance, transport and logistics providers have increased their prices to meet the growing demand for their services because of most economies' "full re-opening" in 2022. Therefore, these high freight costs will likely continue in the first half of 2022. To offset the increases in freight costs, Ugandan manufacturers would ordinarily be expected to increase the prices of their products further.

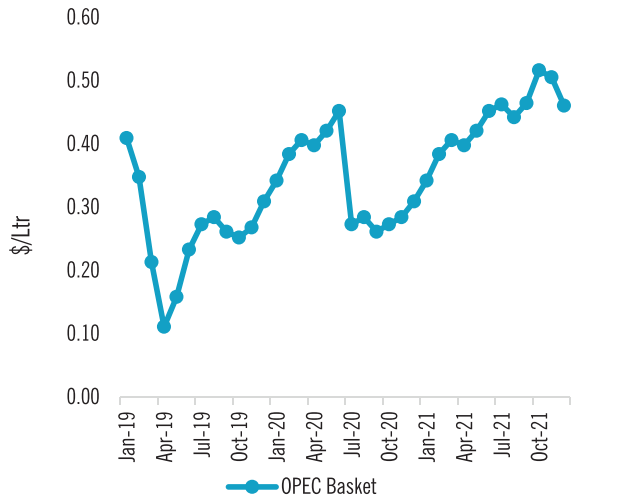
Table 1 Estimated Cost of Producing Cooking Oil in Uganda: June 2021, October 2021, and March 2022

	June 2021		October 2021		March 2022	
	USD	UGX	USD	UGX	USD	UGX
Global Price of Crude Palm Oil (CPO)	1,000	3,560,000	1,400	4,984,000	2,020	7,272,000
Import Duty (10% since July 2021)			*140*	*498,400*	*202*	*727,200*
Infrastructure Levy (1.5% since July 2021)			*21*	*74,760*	*30.3*	*109,080*
Freight cost	101.5	361,340	101.5	361,340	101.5	365,400
Withholding Tax (WHT) on Transport (15%)	15.225	54,201	15.225	54,201	15.225	54,810
Landed cost Kampala	**1,117**	**3,975,541**	**1,678**	**5,972,701**	**2,369**	**8,528,490**
Processing cost	100	356,000	100	356,000	100	360,000
	1,217	4,331,541	1,778	6,328,701	2,469	8,888,490
Processing loss (1.5%)	18.25088	64,973	26.66588	94,931	37.03538	133,327
Net cost of Production	**1,235**	**4,396,514**	**1,804**	**6,423,632**	**2,506**	**9,021,817**
Per Litre	1.122589	3,996	1.640185	5,839	2.278	8,201
LED	0.056	198	0.056	198	0.056	200
Cost of Sales						
Distribution -Litre	0.021	74	0.021	74	0.021	75
	1.199	4,268	1.717	6,111	2.354	8,476
VAT	0.216	768	0.309	1,100	0.424	1,526
Estimated Net Selling Price	**1.41**	**5,037**	**2.03**	**7,211**	**2.78**	**10,001**
Exchange Rate (UGX/USD)	*3560*		*3560*		*3600*	

Source: Author's estimates based on information from Ugandan Manufacturers and international prices of CPO

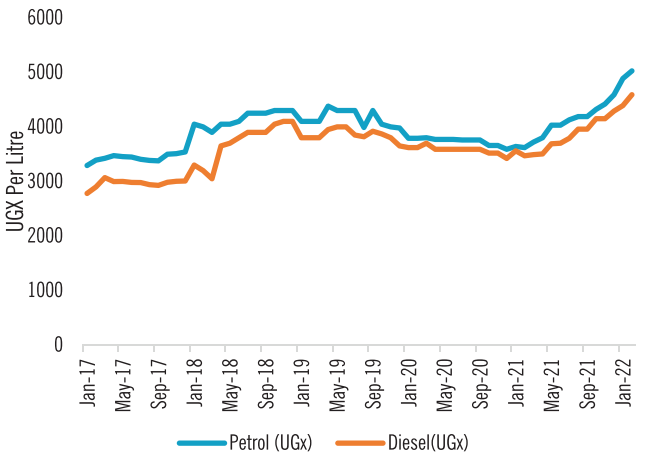
Notes: Estimates assume a constant price for freight, processing, LED and distribution costs.

Figure 11 Trends in international oil prices (USD per litre)



Source: EPRC (2022)

Figure 12 Trends in domestic fuel (petrol and diesel) prices (UGX per litre)



6.4 Increase in the domestic and international fuel prices.

The majority of the manufacturers rely on trucks to transport imported CPO, distribute their final products in the domestic market, and export to regional markets. However, Uganda's domestic fuel prices have escalated in the past six months (Figure 12), which has partly contributed to increases in the transport costs for the manufacturers and retailers. Notably, as shown in Figure 12, the increase in the domestic fuel price is primarily explained by the global crude oil prices (Figure 11).

To cushion the impact of the fuel prices on the cost of production, the manufacturers and retailers have increased the cost of their products; one of the manufacturers intimated that,

> *"In the past, we used the railway to transport CPO from the Mombasa port, but now we entirely rely on trucks – which are more expensive. Therefore, the increase in fuel prices affects the cost of transporting CPO and distributing the final manufactured products. As a business enterprise, this operating cost must be passed on to the consumer, and it is reflected in the price of the laundry soap and cooking oil. (KII, Thursday, March 3rd, 2022)."*

6.5 Decomposition of the retail price to identify drivers

Decomposition analysis was undertaken to apportion the increase in prices between the import duty, the international CPO prices and other costs. A key informant interview with a soap manufacturer revealed that several cost components must be considered. These include but are not limited to the global price of CPO, shipping costs, insurance, tax, inland transport costs from Mombasa, refining costs, packaging costs, and distribution costs of finished products, among others. Given that the international CPO price is the same for both soap and cooking oil manufacturing, the current decomposition examination aimed at establishing how much the price of either one kilogram of soap or cooking oil would be explained by the price of a kilogram of CPO and other costs.[8] In this analysis, the international CPO prices do not include the cost of refining oil, so the refining cost elements are aggregated[9] under distribution, marketing, and manufacturer's costs and margin.

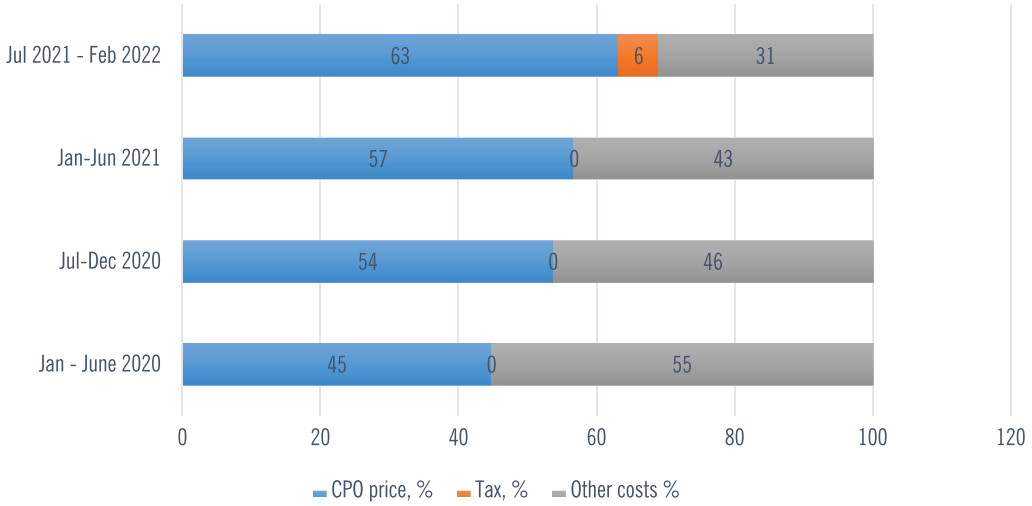
Figure 13 reveals that during the last 2 years, the final price of soap and cooking are, to a great extent, explained by the rising international price of CPO. Specifically, in the first half of 2020 (January – June 2020), CPO prices explained 45 percent of the final retail price per kilogram of either soap or cooking. However, the share of CPO price increased by 9 percent from 45 percent to 54 percent between July – and December 2020. Notably, while the contribution of CPO price to the final retail price for both commodities drastically increased during this period, the absolute final retail price of both soap and cooking oil did not increase by the same measure (Figure 3). Indeed, during the second half of 2020, the average retail price of soap and cooking oil was UGX 3,548 and UGX 7,912, respectively. This situation emanated from the fact that the global price of CPO was much lower during the same period.[10] Therefore, the 9 percent increase in the share of CPO price in the final retail price of both soap and cooking oil was from a low base of absolute international CPO price. Therefore, soap manufacturers did not transfer the considerable increase to final consumers.

8 Because soap and cooking oil are both refined from the same raw material, CPO, which is sold at the same international price. It is practically difficult to disaggregate and apportion one internationally determined price between two final retail products prices, as price of each product's raw material. As such the analysis uses the average of the retail prices of cooking oil and soap. This enables us to examine the cost elements on a weight basis (kg) .i.e. how much does the price of one kilogram of CPO explain in the retail price of one kilogram of either soap or cooking oil?

9 We did not obtain sufficient data to disaggregate refining cost.

10 The average global price of CPO between July and December 2020 was USD 834/MT.

Figure 13 Uganda: Laundry soap and cooking oil retail price decomposition (%), 2020-2021



Source: Author's computation using data from UBOS (2022) and World Bank (2022).

However, further drastic escalations of global CPO prices between July 2021 and February 2022 amidst a new import levy saw the share of CPO in the final retail price drastically increase to 63 percent from 57 in the first half of 2021. As already indicated, the international price of CPO increased by 43.2 percent, from USD 1,063/MT in July 2021 to USD 1,522/MT by February 2022. With this drastic increase in international CPO prices, soap manufacturers transmitted the increased cost of production into the final retail price.

Notably, KIIs with manufacturers attribute the recent drastic increase in final retail prices of both soap and cooking oil to an unfavourable tax environment, characterised by the recent imposition of the import duty and the UGX 200 per litre of cooking oil. However, evidence in Figure 13 reveals that the imposition of the import duty on CPO explained only 6 percent of the final retail price of both laundry soap and cooking oil.[11] From the above findings, it is evident that the recent spike in the retail prices of both cooking oil and laundry soap has been caused by a recent drastic rise in the international CPO price, which is determined at the global level, way beyond the control of the Government.

6.6 Extent of international Crude Palm Oil price transmission to retail commodity price

To understand how much of the increase in the international prices of CPO is transmitted to final retail prices of both cooking oil and laundry soap, pass-through coefficients for different periods between January 2019 and December 2021 were computed.

The findings presented in Table 2 indicate that between January and December 2021, the international price of CPO increased by 28 percent. Moreover, on average, about USD 2 is passed to the final retail prices for every dollar increase in international CPO price (January-December 2021). Considering the pass-through to individual commodities, a more significant share of this global CPO price hike was transmitted into the retail price of cooking oil (pass-through coefficient of 2.6) compared to laundry bar soap (coefficient of 0.8). These findings imply that a unit dollar increase in international CPO price results in a pass-through price of USD 2.6 UGX and USD 0.8 per litre/kilogram of cooking oil and laundry soap bar respectively.

The evidence corroborates KIIs with soap manufacturers, who revealed that soap consumers are more price-sensitive than cooking oil consumers. As such, most manufacturers absorb the high international CPO prices instead of directly transferring it to soap consumers to retain their market share. The pass-through coefficients for January-December 2021 suggest that the international CPO price has been an important factor in explaining the recent surge in domestic retail prices for both soap and cooking oil through price transmission.

11 While KIIs with soap manufacturers indicated that Government recently imposed an excise duty of UGX 200 per litre of cooking oil, however discussions with URA indicated that this excise tax amendment had been in place for the last 3 years (Since FY 2018/19), way before the recent escalation of retail prices for the two commodities. This was further verified through a tax alert located at https://www.pwc.com/ug/en/assets/pdf/ug-tax-watch2018.pdf

Table 2 International price increase pass-through.

Jan/2019 - Dec/2019	Price change/change (USD/Ltr/Kg) [%]	Pass-Through Coefficient
Local price increase: Cooking Oil	(0.001) [-0.069]	(0.008)
Local price increase: Laundry Soap	(0.023) [-2.296]	(0.128)
Local price increase: Average	(0.012) [-0.809]	(0.068)
International price increase: Avg	(0.179) [30.646]	-
Jan/2020 - Dec/2020		
Local price increase: Cooking Oil	(0.158) [7.845]	0.763
Local price increase: Laundry Soap	(0.011) [-1.174]	(0.055)
Local price increase: Average	(0.073) [4.910]	0.354
International price increase: Avg	(0.206) [25.467]	-
Jan/2020 - Dec/2021		
Local price increase: Cooking Oil	0.917 [45.665]	2.300
Local price increase: Laundry Soap	0.218 [22.548]	1.830
Local price increase: Average	0.568 [38.142]	2.065
International price increase: Avg	0.460 [56.812]	-
Jan/2021 - Dec/2021		
Local price increase: Cooking Oil	0.733 [33.435]	2.617
Local price increase: Laundry Soap	0.236 [24.808]	0.843
Local price increase: Average	0.484 [30.825]	1.730
International price increase: Avg	0.280 [28.277]	-

Source: Author's computation using retail prices data and international CPO price from World Bank commodity database.

7. Conclusion and Policy Actions

The evidence presented by the Briefing Note suggests that the recent increase in the prices of domestic commodities, especially laundry soap and cooking oil, is explained by domestic and international factors. The study finds that recent spikes in laundry soap and cooking oil prices are explained to a more significant extent by the recent drastic increase in the global price of CPO and to a small extent by other costs such as the imposition of import duty on CPO imports, a gradual surge in the international shipping costs at sea and the increases in domestic and international fuel prices. Therefore, to provide short term relief, the following policy options could be considered;

i. In the short term, since the primary cost driver for increased domestic retail prices of cooking oil and soap is out of the Government's control, the Government could do nothing and wait for global CPO supply and prices to stabilise as the Ukraine –Russia conflict subsidies.

ii. Alternatively, the Government could temporarily waive the 10 percent tax on the importation of CPO for a short period. This could provide some temporary relief on the cost of production for most soap manufacturers and help stabilise the rapid increase of retail prices as Government also studies the effect of tax waivers on final consumer prices.

iii. To reduce costs associated with the distribution of both soap and cooking oil, there is also a need to explore a fully-fledged cheaper means of transporting CPO from Mombasa to Kampala. In this regard, the Government's ongoing efforts on the Meter-Gauge Railway can be fast-tracked, including its rehabilitation for transportation.

iv. In the medium to long run, the Government should prioritise increasing the domestic production of palm oil, the key raw material for making laundry soap and cooking oil. Here effort should be geared at availing sufficient land to BIDCO to ensure mass plantation and production of CPO.

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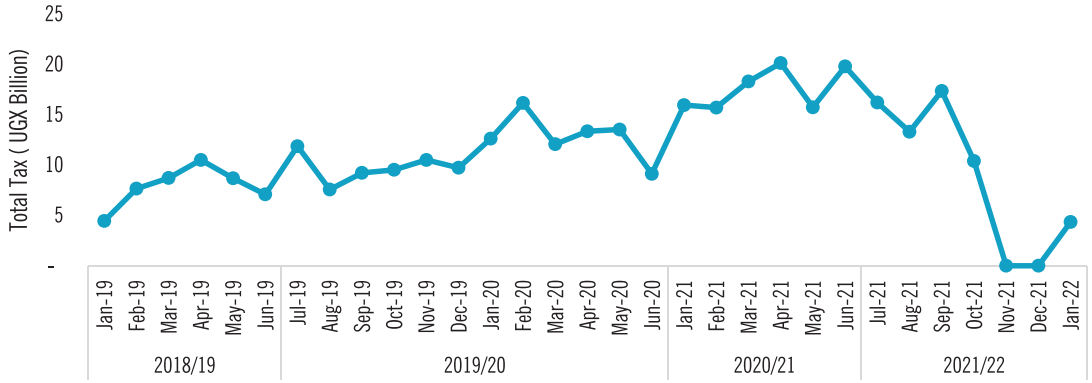
Annex:

Figure A1 Trends in Total Tax revenue from CPO imports (January 2019- January 2022)



Source: Author's computation based on data from Uganda Revenue Authority (2022)

Table A1 Import of crude palm oil and related products. 2019-Jan 2022 (in millions)

		Full calendar year			Jan-June			July-Dec	
Year	Quantity, mt	Value, Ugx	Tax revenue, Ugx	Quantity, mt	Value, Ugx	Tax revenue, Ugx	Quantity, mt	Value, Ugx	Tax revenue, Ugx
2019	593.7	607,519.2	111,731.2	426.7	266,788.2	48,622.6	167.0	340,730.9	63,108.6
2020	167.8	452,670.6	84,599.4	167.8	452,670.6	84,599.4			
2021	219.5	884,554.8	196,787.6	163.3	649,848.8	123,934.1	56.2	234,706.0	72,853.5
2022	4.7	22,252.2	6,948.8	4.7	22,252.2	6,948.8			

Notes: Missing data for July-Dec 2020; and in 2022 data is for January only.
Source: Author's computation based on data from Uganda Revenue Authority (2022) .

Table A2 List of interviewed respondents

No	Name	Company	Mobile number
1	Rwabogo B.W.	Mukwano Limited	0772744743
2	Anoop Sharma	BIDCO Industries	0707792410
3	Francis Baganzi	Nile Agro Group of Industries	0703400188
4	Farida Byenkya	TASCO Group of Companies	0760533551
5	Rajbir Rai	TASCO Group of Companies	0756740040

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Endnotes

1 The teachers could not be traced directly through their schools, since they are not operating during the lockdown and hence could not be accessed through their work places.

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