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SUPPORTING INCLUSIVE GROWTH AFTER COVID-19



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EXECUTIVE SUMMARY

The economic impact of the Covid-19 pandemic on households and businesses in Rwanda has been significant. The impact on low-level income-earning Rwandans and the many small and micro-businesses have been of particular concern.

Data collected by the IPAR-Rwanda show that households in Kigali and Rwanda's secondary cities – such as Musanze, Rubavu and Rusizi – reported that in February 2021, incomes had reduced by 40 per cent on average compared to before Covid-19. At the same time, businesses reported that average turnover and profits were around 50 per cent lower than they were in February 2020 before the outbreak of Covid-19.

There are now however, strong signs that the Rwandan economy is returning to strong levels of growth. In the third quarter of 2021 GDP was 10.1 per cent higher than it was a year earlier, while in the second quarter of 2021 GDP was 20.6 per cent higher than in 2020.

Rwanda in common with many other countries, will have opportunities but also risks in this period of post-pandemic economic recovery. There are two possible paths that future growth could follow. One is where growth is shared widely across the population and the other is where growth is not shared as widely. In this paper, we label these possibilities 'inclusive recovery' and 'unequal recovery'.

The risk of some groups not benefiting from a continued recovery is something that the international literature has identified including; the World Economic Forum, which has warned of what they call a "K-shaped" recovery where the poorest and small businesses would be left lagging behind.

This does not mean that an unequal recovery is inevitable and proactive policy interventions can ensure it is prevented. Rwanda is well placed to ensure an inclusive recovery because of its pre-Covid-19 policies on social protection and its effective economic policy responses to Covid-19, including the Economic Recovery Fund and the Manufacture and Build to Recover schemes.

However, given the scale of the impact of Covid-19 on households and businesses, it will be important

for policymakers to continually to consider how best to ensure a fully inclusive recovery. Covid-19 and its economic impacts have also changed the context and opened opportunities for policymakers.

This paper focuses on policy options that will increase the chances of securing economic growth that is inclusive and making the most of new opportunities opened up by the post-Covid-19 global economy. It draws on primary research conducted by IPAR-Rwanda on the impact of Covid-19 and also on a series of interviews with senior Rwandan policy stakeholders.

The proposed policy options are:

- *Policy option 1:* To help businesses including small and micro enterprises, to access finance more easily: **the initial piloting of and then rolling out of targeted long-term access to finance scheme focused on businesses that will drive inclusive growth – an "Inclusive and Resilient Development Fund"**. Lessons could be taken from the success of the Economic Recovery Fund, as well as attractive interest rates, the scheme could be combined with education and awareness-raising for borrowers to increase financial literacy and ensure all groups are able to access the scheme.
- *Policy option 2:* To further ensure resilient future economic growth; **consideration of additional priority economic sectors for government to target support on**. Three areas to be prioritised for support from the Government of Rwanda are pharmaceuticals and vaccine manufacturing, digital financial services; and Rwanda becoming an e-commerce hub for Central and Eastern Africa.
- *Policy option 3:* To reduce poverty and ensure growth that is more equal: **A debate with employers, on options for increasing and effectively implementing a Rwandan Minimum Wage**. The existing minimum wage is set at 100 Rwf per day and was set as far back as 1970s and could be increased to support inclusive economic growth. Any

introduction of a meaningful minimum wage would require careful consideration and further policy development, and now is the right time for this debate.

- *Policy option 4:* To help reduce input costs for businesses, particularly smaller businesses, to support inclusive growth: explore options including **expanding the Manufacture and Build to Recover scheme into additional sectors and use it to target micro and small firms**, further investments in electricity transmission technology and infrastructure to reduce utility bills.
- *Policy option 5:* To help boost Rwandan SME led industrial development and growth: **introduce tax incentives to new local investors**. Current incentives are mostly targeted at foreign investors. The new Investment Code set out by RDB includes

incentives which will effectively support local investors. Targeting certain Rwandan businesses, such as SMEs or those in job-intensive sectors, could mean tax incentives schemes are both more cost-effective and directly support economic growth that is inclusive.

- *Policy option 6:* To help MSMEs access international markets, **an e-Commerce Recovery Challenge Fund targeted at SMEs in priority sectors could be implemented**. This could be based on a market assessment of which MSMEs have the potential to access international markets including in the context of the AfCFTA. It could bring together the strong existing policies on promoting exports with the Government of Rwanda's focus on e-Commerce for maximum economic and social impact.

(A) ECONOMIC CONTEXT: TWO POSSIBLE PATHS

The impact of Covid19 was significant

The economic impact of Covid-19 has been significant. According to NISR in the second quarter of 2020 – when the pandemic was at its most severe in terms of its social and economic impact – the economy contracted by 12.4 per cent.¹

The IPAR 2021 Survey on business in Kigali & Six Secondary cities indicate that the economic impact of Covid-19 on businesses was large. For example, in February 2021, average sales and profits were around 50 per cent lower than they were in February 2020. The survey also indicates that the Services sector was most severely hit, with median profits in February 2021 down to 60 per cent, followed by Industry (54 per cent) and Agriculture (47 per cent). The data showed no significant variation in the impact of Covid-19 between different genders of business owner.

IPAR-Rwanda have also conducted a survey of households in Kigali and the Secondary Cities, which showed that the economic impact of Covid-19 on households was large.³ In February 2021, households reported that their income had reduced by 40 per cent on average compared to March 2020. This

was consistent for both male and female headed households. To make up for lost income, 81 per cent of households reported that they reduced food consumption, 40 per cent consumed their savings, and 21 per cent sold assets or livestock. Overall, 54 per cent reported that they could not afford sufficient food to meet the needs of their households. When asked to report life satisfaction on a scale of 0-10, households reported that life satisfaction was 4.2 down from 6.5 before March 2020.

Rwanda has recently embarked on a strong economic recovery and measures

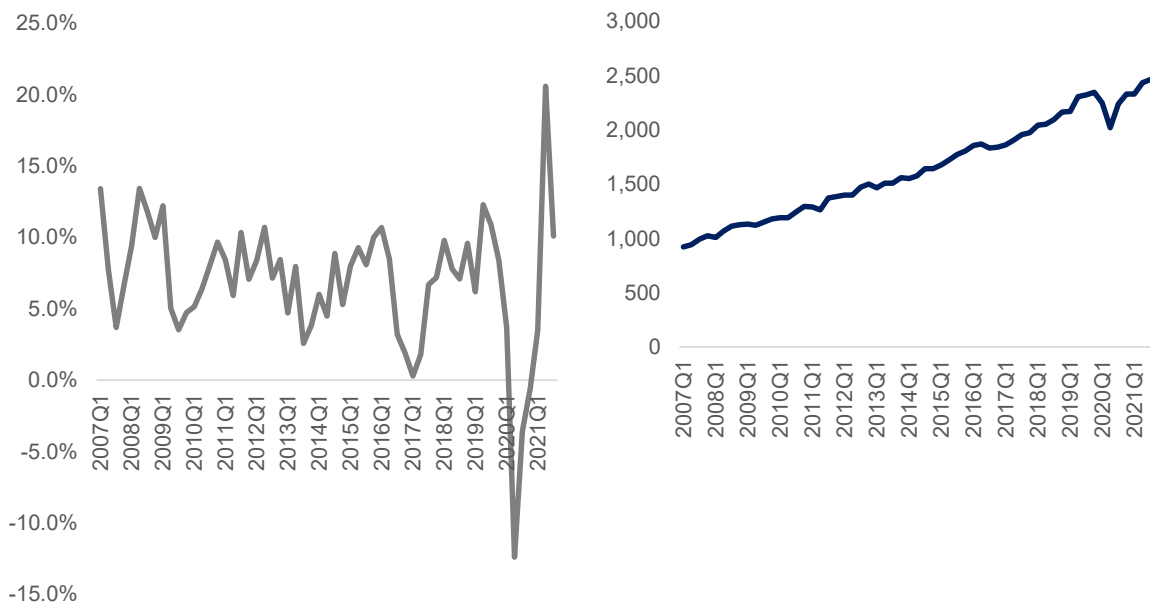
Since the initial economic impact of Covid-19, the economy has rebounded quickly and has returned to strong rates of growth. See Figure 1 below. In the third quarter of 2021, GDP was 10.1 per cent higher than it was a year earlier, while in the second quarter of 2021 GDP was 20.6 per cent (NISR, 2021). As a result of the strong growth rates in recent quarters, the economy has now grown more than it was before the Covid-19 pandemic. In the third quarter of 2021 GDP at constant 2017 prices was Frw 2,464 billion compared to Frw 2,347 billion in the fourth quarter of 2019 (NISR, 2021).

¹ <https://www.statistics.gov.rw/statistical-publications/subject/gdp-quarterly-publications>

² <http://www.ipar-rwanda.org/media/presentations/article/rwanda-s-recovery-from-covid-19-pandemic-preliminary-findings-from-business>

³ <http://www.ipar-rwanda.org/what-we-do/research-policy-analysis/publications/infographic/article/impact-of-covid-19-on-households-in-rwanda-infographic>

Figure 1: GDP growth rates and total GDP, 2007 to 2021

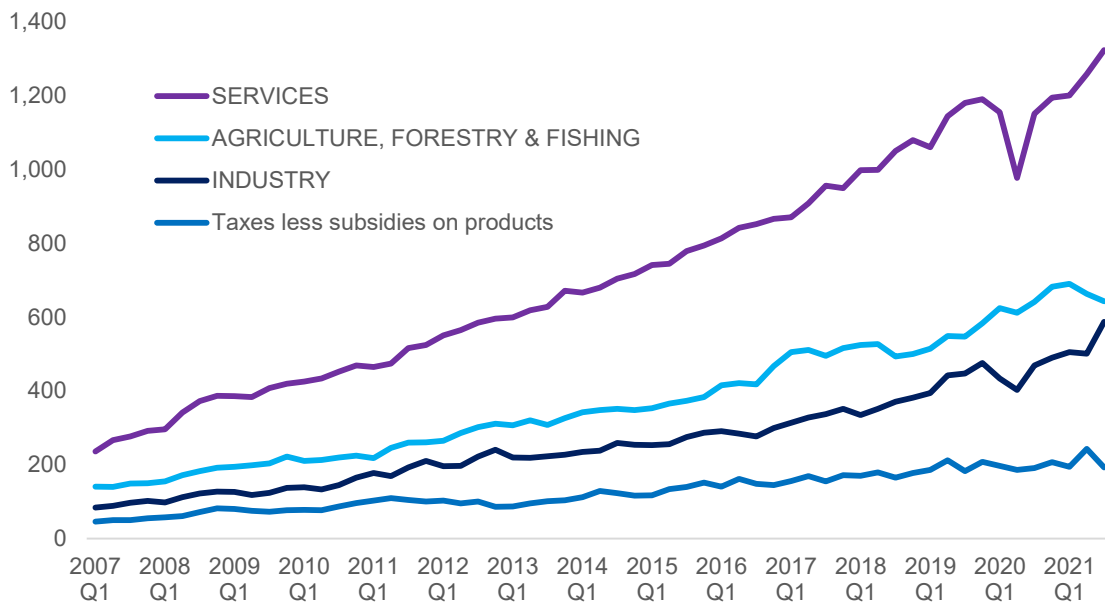


Source: NISR 2021

As Figure 2 shows, the main drivers of this growth have been the Services and Industry sectors. Yearly growth up to the third quarter in 2021 was 25 per cent in the Industry sector and 15 per cent in the

Services sector. The Agriculture sector has not been growing at the same rate: it was the same size in the third quarter of 2021 as it was in the same quarter of 2020.

Figure 2: Contributions to GDP by sector, 2007 to 2021

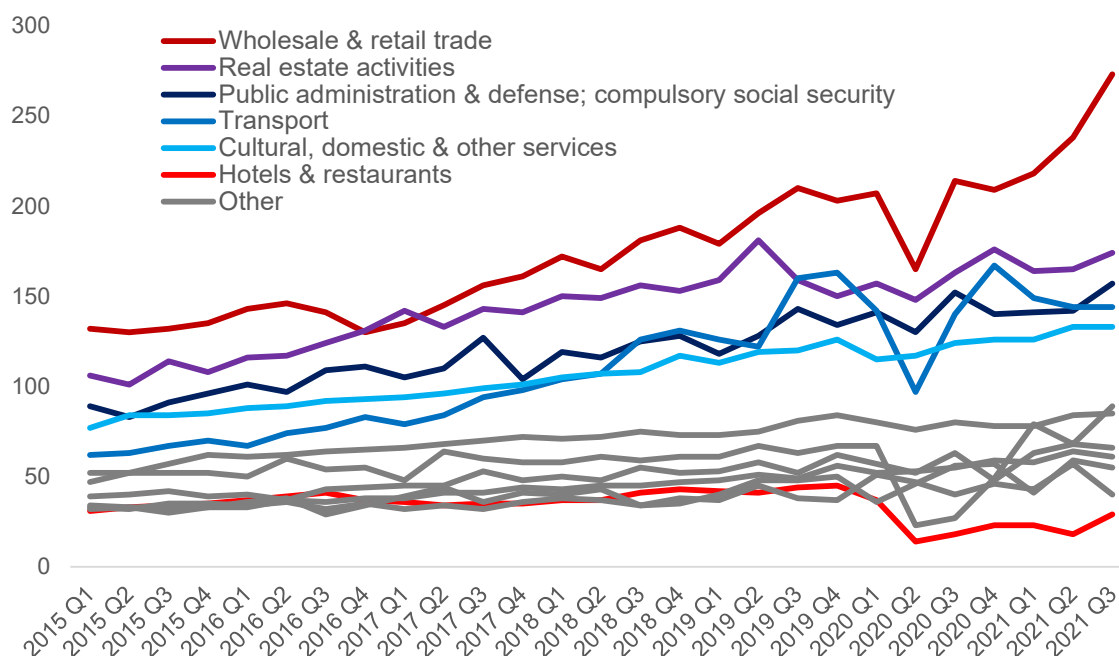


Source: NISR 2021

Within the Services sector, most sub-sectors have experienced growth over the last year. The Wholesale & retail trade sub-sector has grown the fastest. In the third quarter of 2021, it was 28 per cent larger than the previous year. The hotel and restaurant sub-sector

is the only sector which has not recovered since the beginning of Covid-19. In the most recent quarter, its contribution to GDP was Frw 29 billion down from its peak of Frw 45 billion before the pandemic.

Figure 3: Breakdown of GDP sub-sectors within Services, 2007 to 2021



Source: NISR 2021

International debate about “inclusive” vs. “unequal” economic recoveries

In the international literature and debate, there are uncertainties over how economies will recover from Covid-19. There is a live debate over potential ‘shapes’ that recovery could follow. The optimal recovery path is a ‘v-shaped’ recovery. A v-shaped recovery refers to an economy which quickly recovers to its pre-Covid-19 level of output and allows all parts of society and the economy to benefit – in other words it would be an **inclusive recovery**. Early indications based on the overall growth data are that Rwanda’s economy is following the path of a v-shaped recovery.

However, there are other potential paths for economic recovery which need to be avoided. For example, a ‘k-shaped’ recovery is possible. This refers to when different parts of the economy recover at different rates, and one part of the economy recovers quickly while another part lags behind.⁴ Potential areas that could see higher rates of growth during the recovery period include large firms and public sector institutions.⁵ At the same time, smaller firms or people on lower incomes could recover at a slower rate.⁶ This is for a number of reasons; including smaller firms being more vulnerable to insolvency or major financial distress and lack of financial reserves to weather an economic downturn.⁷ This form of k-shaped recovery would not be inclusive, hence an **unequal recovery**.

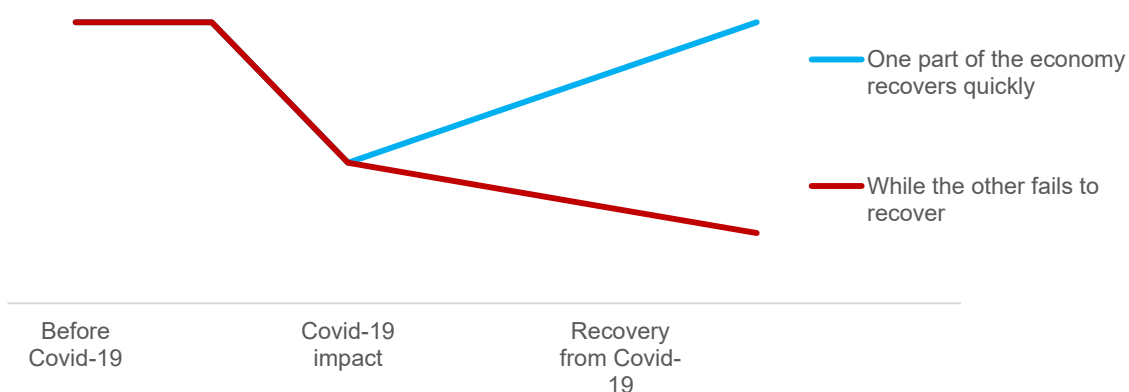
⁴ <https://www.brookings.edu/blog/up-front/2020/05/04/the-abcs-of-the-post-covid-economic-recovery/>

⁵ <https://www.weforum.org/agenda/2020/12/k-shaped-covid19-coronavirus-recovery/>

⁶ <https://www.jpmorgan.com/insights/research/2020-covid19-recession-recovery>

⁷ <https://www.brookings.edu/blog/up-front/2020/05/04/the-abcs-of-the-post-covid-economic-recovery/>

Figure 4: Illustration of a 'k-shaped' recovery



Source: IPAR 2021

Globally, people with lower incomes have in many countries fared worse throughout the pandemic than those with higher incomes, and are at risk of recovering slower.⁸ This is particularly problematic given the evidence on “scarring effects” of recessions: temporary phenomena like unemployment or gaps in schooling have been shown to have permanent effects on living standards.^{9,10} There is no evidence of this happening in Rwanda, but it is important that policy proactively addresses this to avoid a potential k-shaped recovery.

Evidence from IPAR-Rwanda’s survey on households (2021) shows that the average reduction in household income and life satisfaction as a result of Covid-19 has been significant. Therefore, when considering measures to support the socio-economic recovery, it is important to ensure that as much as is possible growth benefits all groups and that none are left behind. Doing so would mean that a k-shaped recovery, or unequal recovery, is avoided, and that a v-shaped recovery, in inclusive recovery, is secured.

The box below outlines the main sources of evidence on which this Policy Brief is based. It reflects insights from IPAR’s own primary research, but also extensive expert input and views from senior policy makers and stakeholders in Rwanda. In the next section, the policy brief outlines the strong policy platform put in place by the Government of Rwanda, and also reports some continued challenges identified by key stakeholders.

Box 1: IPAR Research and stakeholder engagement to support this policy brief

IPAR-Rwanda has engaged in a series of stakeholder consultations to inform this Policy Brief. These were intended to supplement IPAR’s primary data with deeper insights on: i) the challenges being faced by businesses as well as ii) the challenges identified by policymakers. Stakeholder consultations were conducted with senior officials from the Government of Rwanda, civil society organisations in Rwanda, and international organisations.

In addition, IPAR-Rwanda conducted surveys of businesses and households to generate evidence of the impact of Covid-19. For businesses, this included 1545 businesses from three Districts of Kigali City (Gasabo, Nyarugenge, and Kicukiro) and six Secondary City Districts (Huye, Muhanga, Musanze, Rubavu, Rusizi, and Nyagatare). The survey is to be conducted every six months to track the impact of Covid-19 over time. For households, IPAR-Rwanda has conducted a survey of a probability sample of household heads in Kigali and the Secondary Cities. Interviews were carried out on phone due to Covid-19 restrictions. As with the business survey, this will be repeated regularly to track the impact of Covid-19 over time.

⁸ https://www.economist.com/finance-and-economics/2020/09/16/is-the-world-economy-recovering?gclid=EAlalQobChMI4fzumozD9AIVh-vtCh3cGQLEEAAYASAAEgLvivD_BwE&gclid=aw.ds

⁹ <https://www.epi.org/publication/bp243/>

¹⁰ <https://esrc.ukri.org/about-us/50-years-of-esrc/50-achievements/unemployment-scarring/>

(B) POLICY CONTEXT: KEY FOUNDATIONS TO SUPPORT AN ECONOMIC RECOVERY

The strong policy response to the economic impacts of Covid

The Government of Rwanda has been effective at bringing in a range of measures to support businesses and households dealing with the effects of Covid-19. This is generally be split into two categories of responses.

The first category was support during the time of severe economic contraction, for example when strict lockdowns were in place to prevent the spread of the virus. This support included increased healthcare spending and social protection interventions to directly support households. It also included a range of measures to support businesses including delaying tax payments, regulatory relief for financial institutions, and reduced transaction fees on mobile payments. These measures were analysed by IPAR-Rwanda's data analysis that was published in September 2021.¹¹¹²

The second category of intervention aimed to support businesses and households recover and grow once the economic effects of Covid-19 are less severe. This policy brief focuses on this second type of support. Key interventions the Government of Rwanda has introduced in this second type are i) the second round of the Economic Recovery Fund (ERF) and ii) the Manufacture and Build to Recover programme (MBtR).

The second round of the ERF will add an additional Frw 250 billion to the Frw 100 billion already committed in the first phase.¹³ Key differences from the first round of the ERF include less restrictive eligibility criteria to attract a larger number of businesses, allowing the money to be used for investment purposes that will cover more sectors including transport and education.

The MBtR programme has been introduced to support the manufacturing and construction sectors. Specifically, the programme targets agro-processing, light manufacturing, and construction materials.¹⁴ It supports businesses in these sectors through tax breaks and tax credits. The MBtR programme has been implemented effectively and already exceeded its target level of investment, with an estimated USD 1.2 billion attracted across 78 investors.¹⁵

Box 2: Economic Recovery Fund (ERF)

The ERF was established by the Government of Rwanda to enable businesses affected by Covid-19 to resume and sustain operations and preserve jobs (RDB, 2021). Total funding for the first round was Frw 100 billion (USD 100 million).

The first round of the ERF had windows for hotel refinancing; working capital/line of credit; microbusiness; and a guarantee scheme. Loans were given with 8 per cent interest rate to borrowers and lenders could access the finance at 0 per cent interest rate.

The ERF has since been expanded to Rwf 350 billion. In the second phase of the ERF the fund has been adapted in a number of ways. These include:

- Reduced eligibility criteria – for the first round of the ERF, businesses had to show that turnover had declined before Covid-19. Removing the criteria will mean new businesses can use the ERF.
- Wider sector eligibility – the first round of the ERF was focused on supporting those sectors most affected by Covid-19, in particular hotels. The second round will allow businesses from a wider range of sectors to access the funding, including transport and education.

¹¹ <http://www.ipar-rwanda.org/what-we-do/research-policy-analysis/publications/briefs/article/policy-brief-rwanda-s-post-covid-19-economic-recovery-the-role-of-e-commerce>

¹² <http://www.ipar-rwanda.org/media/presentations/article/rwanda-s-recovery-from-covid-19-pandemic-preliminary-findings-from-business>

¹³ <https://www.gov.rw/blog-detail/prime-minister-presents-to-the-parliament-rwandas-economic-recovery-plan>

¹⁴ <https://www.newtimes.co.rw/news/new-incentives-local-manufacturers-explained>

¹⁵ <https://www.newtimes.co.rw/news/incentives-manufacturing-attract-12bn-investments>

- Funding for innovation – a substantial part of the first round of the ERF funded day-to-day expenditure for businesses. The second round allows businesses to use finance for investment purposes.
- Larger loans for smaller businesses – small and medium sized businesses could borrow a maximum of Rwf 1 million over two years in the first round of the ERF. The second round will allow up to Rwf 5 million to be borrowed over a period of 3 years.

These changes in the second round of the ERF reflect the changing nature of the support that is being provided. Earlier on in the response to Covid-19, support needed to ensure businesses could survive in the short term. It is important that support allows businesses to invest and grow in the recovery period from Covid-19.

As well as a number of adaptations, there are a set of principles from the first round of the ERF which are being maintained. **The central intervention is still providing finance at a lower interest rate than the market will provide.** Equally, loans to small and medium sized businesses will continue to be delivered through the Business Development Fund (BDF). BDF has demonstrated that it can effectively deliver finance to a range of firms across Rwanda, for example by working with Savings and Credit Cooperative Societies (SACCOs).

These programmes have played an important role in ensuring the Rwandan economy weathered the period of the pandemic's most extensive impact on the economy, and is now in a position to ensure a return to growth.

The Rwandan context: continued challenges and opportunities from Covid-19 disruption

Based on IPAR-Rwanda's consultations with key stakeholders, some challenges and opportunities for maximising the degree to which future Rwandan economic growth is inclusive were identified. These include:

- **The importance of supporting micro and small businesses as part of a strategy to ensure an inclusive and resilient economic recovery.** This is because SMEs provide a large proportion of employment in Rwanda (NISR, 2020). Data from NISR further show that among enterprises in 2020 over 68 per cent of employment came from micro and small enterprises. Supporting small and micro-businesses also leads to spill-over effects in the economy, for example, higher wages lead to increased consumption which has a positive spiral effect to create more jobs.
- **Micro and small businesses' access to finance** was a common theme in IPAR's consultations. Accessing finance allows businesses to make use of more capital than they currently own. Using this to invest in items like new machinery, inputs, or innovative activities more generally, means businesses can grow faster than they otherwise would. Allowing growth for individual businesses this supports the overall growth of an economy. Challenges in accessing finance were reported to be particularly significant for smaller businesses, which tend to find it more difficult than larger firms to get the collateral required for loans, or to negotiate the procedural requirements to borrow.
- **High input costs, which disproportionately affect smaller businesses.** For example, costs of transport and logistics were high, especially during the period of restrictions caused by Covid-19. This makes it more difficult for businesses to operate and reduces profit. The effect of high and increasing inflation globally means that input costs for businesses are likely to continue to be a challenge for businesses.¹⁶ The Government of Rwanda has already taken measures to reduce the impact of global inflation by intervening to reduce fuel costs, including the removal of VAT from petroleum products.¹⁷
- **Access to international markets:** A third challenge was for businesses to access and operate in international markets. Engagement with stakeholders revealed that

¹⁶ <https://www.newtimes.co.rw/international/eurozone-inflation-hits-13-year-high-34>

¹⁷ <https://www.newtimes.co.rw/news/how-govt-fuel-subsidies-are-curbing-inflation>

while large firms are often able to access international markets, for smaller firms this can be more challenging. Increasing trade and access to regional markets for firms across the economy could be an effective way to increase exports and increase economic growth.

- **Potential opportunities in new economic sectors:** While businesses are facing significant challenges during the period of economic recovery, there are also

opportunities that have opened up as a result of the changes induced by Covid-19. The most obvious example of this is increased demand for certain products, such as vaccines or personal, protective equipment (PPE). Other examples include increased demand for technology services and lower supply of certain inputs. These changes provide potential opportunities for new sectors to develop in Rwanda, which could be supported by government intervention or support from development partners.

C. GOING FURTHER DOWN THE INCLUSIVE GROWTH PATH: POLICY OPTIONS

As detailed above the economy is showing strong signs of growth across a wide range of sectors. The measures introduced by the Government of Rwanda have been effective at driving this growth and leading to a fast rebound from the economic impact of Covid-19.

To ensure that growth is sustained and is resilient to future potential shocks, some policy options have been developed below. As well as securing resilient economic growth, these are designed to mitigate against the potential for a k-shaped recovery from Covid-19 and ensure economic growth is sustainable and inclusive.

In general terms, supporting labour intensive sectors and sectors with a higher proportion of lower paid jobs can be an effective way to achieve the goals of eradicating extreme poverty by 2024 and accelerating inclusive economic growth as set out in NST1. This is already being done effectively, for example through the Manufacture and Build to Recover scheme. There are additional measures for consideration that could lead to further progress towards the NST1 targets which are set out below.

Policy option 1: a targeted long-term access to finance scheme focused on businesses that will drive inclusive growth – an “Inclusive and Resilient Development Fund”

Access to finance has been identified as a major challenge for businesses during recovery from the

effects of Covid-19. Interviews with key stakeholders suggested small and micro businesses, as well as those in rural remote areas, faced greater challenges in accessing finance.

An access to finance scheme that targets these businesses could be an effective way to increase economic growth that is inclusive. Such a scheme should use the lessons developed from successful implementation of the Economic Recovery Fund. Key lessons from successful implementation of the ERF include i) providing an interest rate that is attractive to borrowers and still leaves enough profit for lenders, ii) delivery through SACCOs and BDFs to reach a wide range of potential borrowers and iii) requiring funding to be used for investment purposes rather than to finance day-to-day spending.

The Government of Rwanda have already implemented a scheme which targets the small livestock sub-sector including poultry, pig farmers and animal feed producers.¹⁸ Using similar principles on an expanded scale, a scheme which focuses on small and rural businesses throughout the economy could ensure that economic growth does not leave any group behind, while embracing inclusive financial access and enhancing rural productivity.

Further analysis could be conducted to identify criteria that would most effectively support inclusive growth, but potential criteria might include:

- Small businesses and household enterprises

¹⁸ <https://en.igihe.com/news/article/poultry-pig-farmers-and-animal-feeds-producers-to-benefit-from-subsidized>

- Operate in a rural area
- Number of additional jobs that could be created as a result of the lending

As well as attractive interest rates, the scheme could be combined with education and awareness raising for borrowers to increase financial literacy and ensure all groups are able to access the scheme. This could include forums held on a regular basis to explain the responsibilities of the financial sector as well as requirements for lenders to provide basic financial information in an accessible manner. Increasing financial literacy in this way would increase the likelihood of the scheme supporting economic growth which is inclusive.

To ensure that a future scheme is an effective use of public money, pilots could first be conducted which test the intervention on a small scale. Doing this before fully rolling out a scheme would allow evidence from real-world performance to feed into scheme design and ensure that potential delivery challenges are identified in advance.

By conducting a pilot scheme now, evidence could be gathered which can inform **creation of a new “Inclusive and Resilient Development Fund” which is ready to begin on a larger scale when the ERF comes to an end in the coming years.** By building on the lessons of the ERF, new access to finance scheme could continue to support inclusive growth. Being highly targeted would mean scheme costs are kept relatively low.

There are other initiatives underway which may provide lessons on how to improve access to finance particularly for people of lower incomes. For example, MTN Rwanda has recently introduced a function where customers can save relatively small amounts through their mobile phones. Customers are then able to borrow money using these savings as collateral. Digital financial services of this kind could be an effective way to allow low-income groups – who would otherwise struggle to access finance – to borrow money. Lessons from the MTN Rwanda scheme could be applied to microfinance institutions or Savings and Credit Co-operative Societies (SACCOs).

Policy option 2: consideration of additional priority economic sectors to increase the resilience of economic growth

The Government of Rwanda has got effective policies to support priority economic sectors. Sectors such as tourism and hospitality have been supported and have been strong drivers of growth. During Covid-19, an increased focus was placed on supporting new sectors such as manufacturing and construction through the Manufacture and Build to Recovery (MBtR) scheme. Since these sectors support a large number of workers this support is likely to support inclusive growth which benefits a wide proportion of the economy.

Further support is provided by the new Investment Code as set out by RDB. This includes development of Kigali Innovation City and the Kigali International Financial Centre, as well as support for film production and post-production and mining exploration. The Investment Code also explains the increasing flexibility of Cabinet who have the authority to approve special incentives for strategic investment projects. This allows more flexibility in reaching national targets and responding to shifts in global trends.

Given the disruption caused by Covid-19, there are two reasons why there is a case to build on the support provided to priority sectors.

The first is to increase the extent to which economic growth is inclusive. Specific measures that could be implemented to achieve this are i) to require local contractors to conduct activity which is commissioned by the Government of Rwanda and ii) focus on support to labour-intensive activities. Labour intensive activities are already being supported effectively through the Manufacture and Build to Recover scheme. By building on this principle and expanding support to other labour-intensive activities, an even larger number of workers could be supported.

The second is to increase the resilience of economic growth. Covid-19 showed that certain sectors can be particularly prone to any single economic crisis, for example, the hotels & restaurants sub-sector still has not yet recovered to its pre-Covid-19 peak as shown in figure 3. By supporting growth that is driven by a wide range of sectors, economic growth is more likely to be sustained even in periods of global economic shock. The Covid-19 pandemic has also opened up new economic opportunities as a result of the changes it has brought to daily lives around the world.

Given Rwanda's existing strengths and the global economic environment emerging after the harsh impact of Covid-19, there are at least three sectors that are strong contenders to be prioritised for support from the Government of Rwanda. These are:

- **Pharmaceuticals and vaccine manufacturing** – developing the pharmaceutical industry and manufacturing of medical equipment is a priority set out in NST1. The Covid-19 pandemic has meant that there are even greater economic opportunities associated with the production of medical products, in particular vaccines. Rwanda is in a strong position to develop vaccine manufacturing capabilities, and Pfizer has recently announced they intend to build a vaccine manufacturing plant in Rwanda.¹⁹ Government support can ensure that the sector is able to flourish, for example by ensuring regulations facilitates high-quality manufacturing processes and exports. It is also important that the opportunity is used to ensure skills are developed locally, for example by building the capacity of Rwandans in the fields of pharmaceuticals.
- **Financial services** – the Government of Rwanda are already effectively providing support to expand the provision of financial services. One example of this is through the creation and growth of the Kigali International Financial Centre. Support could be strengthened in a way that increases the effect on driving economic growth which is inclusive. To ensure that expanded financial services can be widely accessed, initiatives to increase financial and digital literacy could also be implemented.
- **E-Commerce hub** – becoming a hub for e-Commerce would attract businesses to Rwanda in order to access regional and continental-wide markets. Rwanda has a strong foundation in the infrastructure required to be a hub for e-commerce, for example, good ICT infrastructure and high-quality internet services. The AfCFTA protocol on e-Commerce also means the benefits from becoming an e-Commerce hub are likely to be even greater in the future. Supporting the e-Commerce sector to continue to grow could be an effective way to build

resilience to the economy and support inclusive growth. Ensuring that the sector develops in a way that builds local skills in the areas of digital and ICT would increase the availability of high-skilled jobs.

Policy option 3: New debate, including in consultation with employers, on options for reviewing, revising and effectively implementing a Rwandan Minimum Wage.

Minimum wages can be an important *part* of policy makers' approach to ensuring inclusive economic growth. They both help reduce poverty, by providing a minimum income for workers and also help reduce income inequality.²⁰ Most countries, including developing countries and other countries in sub-Saharan Africa combine a minimum wage which would ensure workers are at the very least above the extreme poverty line (of USD 1.90 per day).

They will only ever be *part* of the policy response to poverty and inequality for several reasons. The cost of a minimum wage falls on businesses as well as government. Minimum wages by definition only benefit workers in the formal sector. And linked to that, in developing countries, incomes for many households do not come from wages. An important policy question in most countries is what the balance should be between on the one hand government social protection policies – including the payments of cash transfers or other approaches to protecting poor households' livelihoods, and on the other hand minimum wages paid by employers.

The existing minimum wage is set at 100 Rwf per day and was set in the 1970s.²¹ In 2018 a new labour law was passed, which did include some important extensions an employee entitled to. However, this did not increase the minimum wage.²²²³ Since the 1970s, inflation has further eroded the value of the Rwandan minimum wage. Rwanda's existing minimum wage does not even allow recipients to receive an income above the extreme poverty line.²⁴

The current period of economic recovery from Covid-19, coming on top of robust economic growth in Rwanda before Covid-19 for several years, is a good time for policymakers to consider the options

¹⁹ <https://www.nature.com/articles/d41586-022-00335-9>

²⁰ https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/documents/publication/wcms_762302.pdf

²¹ <https://www.newtimes.co.rw/news/why-are-we-stuck-minimum-wage-set-40-years-ago>

²² <https://www.newtimes.co.rw/news/labour-law-minimum-wage>

²³ <https://www.ulandssekretariatet.dk/wp-content/uploads/2021/05/LMP-Rwanda-2021-Final.pdf>

²⁴ https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/---publ/documents/publication/wcms_762534.pdf

for introducing an appropriate minimum wage. It could make an important contribution to ensuring as inclusive as possible a growth trajectory in future years. As in any country, such a policy move would need careful consideration in Rwanda. Some key policy considerations include:

- *Uniform vs. sector-specific minimum wages:* some countries opt to set minimum wages at different rates depending on the economic sector. This reflects the different potential trade-offs in different sectors between minimum wage rates and job numbers. There is a strong case for sector-specific rates.
- *How should rates be set:* the process of setting rates generally requires independent expert advice and then a system of consultation and dialogue with both representatives of labour and employers. This form of social dialogue was recently described as being in progress in Rwanda with tripartite institutions (representatives from government, business, labour) meeting regularly.²⁵ The mechanism for deciding on rates would need careful consideration.
- *Options for covering the informal sector:* One challenge with minimum wages is ensuring they can be implemented in both formal and informal employment. While informal businesses may not be registered with the Rwanda Revenue Authority (RRA) and other regulatory bodies or keep formal accounts, there are other mechanisms that could be used to increase the likelihood of successfully implementing a minimum wage in the informal sector. For example, local administrative entities could monitor wages from sector to cell levels.

These policy design questions would need careful consideration. It is likely that the introduction of a meaningful minimum wage would need to be incremental, ensuring firms are able to adjust if necessary. However, a serious debate about the minimum wage is long overdue. Detailed further policy thinking could be an important next step. As part of Rwanda's wider approach to social protection and poverty reduction, a new Rwandan Minimum Wage, could be an important contribute to more equal growth in future years.

Policy option 4: reduce input costs to support inclusive growth

High input costs to businesses were identified as a key challenge for businesses in Rwanda in IPAR-Rwanda's business survey, 88 per cent of businesses reported input purchases in their top three reasons for needing support in the recovery from the economic impact of Covid-19. Transport and logistics were identified as particular challenges in follow up consultations with stakeholders.

Measures the Government of Rwanda took during Covid-19, for example subsidies to transport fares and tax relief on vehicle imports, were effective ways to reduce the impact of high input costs on businesses in the transport and Meetings, Incentives, Conferences and Exhibitions (MICE) sectors. Equally the Manufacture and Build to Recover (MBtR) scheme has been effective at increasing investment in the construction and manufacturing sectors by reducing tax payments on inputs.

A future scheme which reduced input costs to certain businesses could be an effective way to support inclusive growth. One way of doing this could be to **expand the Manufacture and Build to Recover scheme into additional sectors and use it to target micro and small firms**. Doing this could be an effective way to support a large section of the economy and those who are more likely to be on lower wages.

There are other interventions that could reduce the input costs for businesses. For example, utilities (energy and others) could be reduced through further investments in energy transmission technology and infrastructure.

Policy option 5: tax incentives to local investors

Tax incentives can be an effective way to stimulate investment. The Manufacture and Build to Recover scheme **has attracted USD 1.2 billion through 78 investor applications**, exceeding its target of around USD 1 billion.

Companies registered to operate as free trade zone developers or foreign companies with headquarters in Rwanda currently benefit from tax relief. These include relief on corporate income tax, for which they pay zero percent; exemptions from withholding tax; and tax-free repatriation of profit.²⁶

²⁵ <https://www.ulandssekretariatet.dk/wp-content/uploads/2021/05/LMP-Rwanda-2021-Final.pdf>

²⁶ A guide to taxation in Rwanda. 2015 tax facts and figures: <https://www.pwc.com/rw/en/assets/pdf/taxguide2015-rwanda.pdf>

In the future if the GoR is to widen the tax base, it would be necessary to attract the individual local investors whose investment can employ more local experts with tax relief benefits for a period of 3 -5 years. As of now, local investors have to pay a corporate income tax of 30 percent or withholding tax of up to 15 percent.²⁷

Extending tax incentives to local investors could be an effective way to boost industrial development. Doing so in a way that targets certain businesses, such as SMEs or those in job-intensive sectors, could mean such a scheme is both more cost-effective and more directly supports economic growth that is inclusive.

Policy option 6: support for SMEs to increase exports and access international markets through e-Commerce, including for smaller businesses

Rwanda has established policies to effectively support businesses to access international markets. For example, in the case of agricultural exports the National Agricultural Export Development Board (NEAB) provides packages of support for new or early stage exporting businesses in priority sectors. The sectors include traditionally strong Rwandan exports – including tea and coffee – as well as newer sectors with growth potential, such as horticulture.

Within these priority sectors the existing approach rightly emphasises the provision of a package of support for firms, which will help overcome the range of potential barriers to expanding exports. This includes support across securing necessary investments; the quality of production and productivity of potential exporters; branding; freight and logistics costs (see above); and business incubation support.

As the economy recovers from the economic impact of Covid-19 there is a case for expanding the focus on all these forms of support for SMEs with the potential to increase exports. There is, however, also a case for increased focus on e-Commerce to help connect exporters to international markets – creating market linkages.

The Government of Rwanda have an excellent platform to build from. Plans already included using Alibaba’s e-Commerce platform for the sale of coffee and other products to China. The aim was already to increase market penetration beyond wholesalers (for example direct to small outlets such as shops, or direct to consumers).

Given the economic impact of Covid-19, and the boost this has given to e-Commerce globally, there is a case for expanded focus on supporting new exporters to use e-Commerce. There is a particular opportunity for new and small exporters who may not be able to trade in volume to wholesalers.

Further research and analysis in this area could be useful. This might include:

- a) A post-Covid-19 market assessment to explore the pattern of new business start-ups with the potential or ambition to access export markets
- b) An e-Commerce Recovery Challenge Fund targeted at SMEs in priority sectors. This could be based on the market assessment and comprehensively bring together the strong existing policies on promoting exports with the Government of Rwanda’s focus on e-Commerce for maximum effect.

²⁷ https://www.netherlandsandyou.nl/binaries/netherlandsandyou/documents/publications/2021/06/18/doing-business-in-rwanda/PayingTaxesinRwanda_202002.pdf

D. CONCLUSION AND NEXT STEPS

As with many countries, the impact of Covid-19 on the Rwandan economy has been significant. The Government of Rwanda introduced a range of measures to effectively support businesses and households when the effects were heightened. More recently, the Government of Rwanda has also introduced schemes to support businesses to grow in the period after Covid-19's most significant impacts, in particular, the second round of the Economic Recovery Fund and the Manufacture and Build to Recover scheme. Together, these packages of support have been effective, and the economy has returned to high levels of growth.

While there are strong signs that the economy is recovering and will continue to do so over the coming years, it is important that this economic

growth continues to be as widely shared across the population in Rwanda as possible. Globally, there are signals that the economic recovery from Covid-19 could be 'k-shaped' with some groups of the population not benefiting. It is too early to tell whether this might be happening in Rwanda, but it is important that policymakers continue to debate proactive policy measures which would prevent this possibility from occurring. This policy brief sets out some options for doing this.

IPAR will continue to monitor the impacts of Covid-19 through its regular surveys of businesses and households. In summer 2022 IPAR will be publishing its second round of analysis of the business survey, and will subsequently be publishing data from its first round of the household survey.

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