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Towards Sustainable Development

POLICY BRIEF

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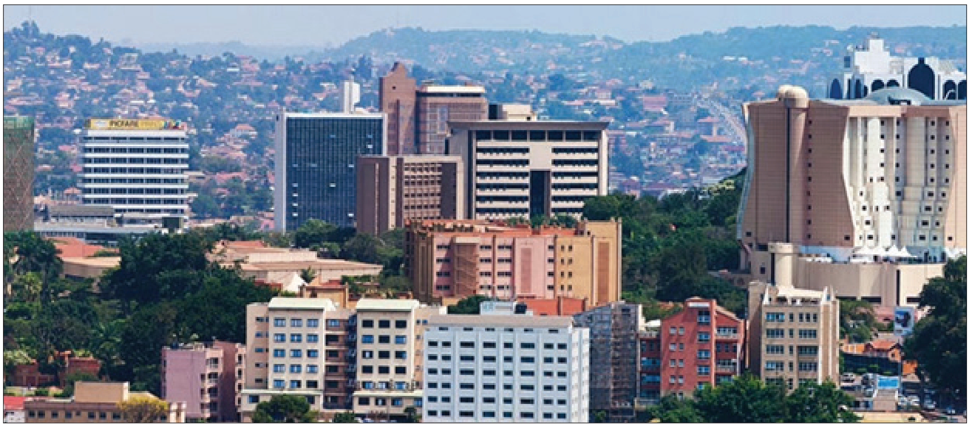
Improving the growth and transition of small and medium enterprises in the Greater Kampala Metropolitan Area.

Executive summary

Urban areas in Uganda are increasingly facing competition for their resources in the face of rising population. More than one out of every five Ugandans are residing in urban areas and the urban population is expected to triple in next two decades. Most of the urban population resides in GKMA—a region challenged with unemployment and inadequate opportunities. Enhancing firm performance in urban areas offers a promise for jobs and local revenue to boost city development. Local governments and city council need to create mechanisms that address firm constraints and harness the factors that drive firm competiveness, growth and transition. Potential opportunities lie in collaborating with financial institutions to provide affordable credit, improving taxation procedures, establishing of business spaces for the small firms and influencing vocational schools to impact relevant skills.



Introduction

Increasing the local economic performance of urban centers to match the ever increasing competition for their resources is a growing concern for policy makers in Uganda[1]. Several cities and townships have rapidly expanded beyond their initial confines bringing with them the problems of unplanned settlements and slums, congestion, poor sanitation and pollution, and unemployment triggering urban poverty. These structural and socio-economic problems are experienced more in the Greater Kampala Metropolitan Area (GMKA) which is a home for more than one fifth of the urban population[2] with Kampala city alone housing 21% [3]of those inhabitants . Uganda's urban population is projected to triple in the next two decades implying that urban development in GMKA must create more opportunities if it is to cater for the growing numbers.

Promoting firm growth in urban areas may offer a solution to the urban challenge. Firms are often the starting point of urban growth because they provide basic goods and services and jobs thus contributing to local economic development and transforming livelihoods[4]. Large firms are known to create high quality jobs which enhance productivity while Micro, Small and Medium-sized enterprises (MSME) can absorb productive resources at all levels of the economy stimulating the creation flexible economic systems in which small and large firms are interlinked. Thus are critical in bridging the rural-urban divide by facilitating the transition of agricultural to industrial production by providing processing opportunities whose activities further generate local revenue. The fact that MSMEs account for majority of the firms in Uganda[5] could easily help the country achieve these benefits especially since they are labor intensive and create employment with relatively low levels of investments. They are also effective in the utilization of simple and affordable technologies which are easy to adapt and transfer. However, firms in urban cities face several market failures which constrain their performance growth, and transition. This brief highlights these constraints and interventions needed to address firm deficiencies and enhance their competitiveness to promote more sustainable local development of GMKA.

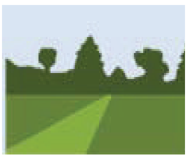
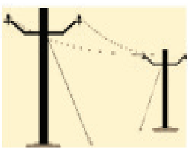
The study

This brief examines constraints to small and medium firm's business operation in the GKA. It is based on a qualitative study titled "*Barriers to firm expansion and transition in Greater Kampala Area*" conducted by EPRC and in the London School of Economics (LSE) with support from the World Bank.[6] The study interviewed 80 micro, small, medium and large firms in Kampala, Mukono and Wakiso districts. In addition, the study interviewed Ministries Departments and Agencies (MDAs) and private sector agencies from the above localities.

Constraints to business operations

The table below presents the various major barriers experienced by small, medium and large firms which increase the cost of doing business affecting their productivity and growth in GMKA. In addition to these firms cite poorly regulated market unable to detect the quality of products on the market, poor entrepreneurship skills, crime and theft from employees and a lack of raw materials which affect production.

Firm Constraints and their impact on business operations

Constraint	Small firms	Medium and Large firms
Finance 	A lack of capital in turn limiting business operations and acquisition of assets for production. Credit from banks is not sufficient, carries high interest rates and is short-term.	Banks offer short term and expensive credit to match business goals and encourage growth and expansion. The process of obtaining these loans is cumbersome, slow and not -standardized.
Transport 	Lack of means of transportation and poor roads which lead to damaging of products and thereby increasing costs of operation	Poor roads limiting access to markets of both raw materials and sale products. Bad roads increases the costs of vehicle maintenance and reduce available capital for production
Land 	Procedures of acquiring space and rights especially in Kampala city are not entirely clear, costly and demand so much time. The process requires several documents.	The cost of procuring land is high and demands substantial capital. This is worsened by multiple land tenure system. Land acquisition for expansion is often through informal relationships. Thus the process of establishing the real owner is complex and cases of fraud by sellers of land are common.
Electricity 	Poor quality and power distribution which affects timely production and in turn firm productivity.	High costs of power. The cost of 0.04 USD/ kilowatt hour is twice the average costs of Sub-Saharan Africa. The quality of power is poor and unstable damaging machines and increasing operation costs thus limiting firm growth.
Unfair competition 	We have to compete especially with foreign investors owning large firms making similar products and manufacturing in large quantities. Their presence is crowding out the small entrepreneurs.	Suffer competition from foreign investors and informal firms who make poor quality products and sell at lower prices

Constraint	Small firms	Medium and Large firms
Technical skills 	A lack of skilled labor which affects timely delivery of quality outputs and higher productivity. There is generally a lack institutions prepared to equip students with appropriate skills to produce goods for the bigger markets. Most employees are trained on job and this is costly. In addition, it discourages encourage expansion and transition.	There is a limited supply of employees with appropriate technical skills and a good working culture and ethics. The labor market in Uganda is characterized by a high labor turnover and this increases the cost of training and capacity building.
Taxation 	Businesses pay a number of dues and taxes that are a burden to their growth. Firms lack knowledge and awareness of the tax system and face difficulties in understanding the complex tax codes including the new online systems. In addition the high-handed approach by tax collectors in local government authorities discourages compliance.	Imported raw materials are taxed increasing the cost of production which renders domestic products expensive compared to the foreign manufacturers. There also multiple taxes whose costs are passed to the consumers. In addition mechanisms of receiving tax exemptions is not clear as some firms of similar business may be exempted and others not. Tax breaks and other incentives are offered to mainly large and foreign firms. Furthermore government is weak on taxing informal businesses that remain invisible to regulations.

Policy interventions

The above barriers, challenge local governments and stakeholders to identify strategies through which GMKA can secure and manage resources and investments that drive firm competitiveness in line with the changing city. Interventions that may be pursued by KCCA and the Municipals of Mukono and Wakiso districts could encompass;

- Facilitating financing for businesses whereby they work closely with banking institutions to reduce the pricing for small firms and creating guarantor programs for businesses that do not have all the traditional requirements demanded by banks. Facilitating the bankability of these enterprises to create greater access to finance. The need to encourage businesses to join associations and that have information on business grants and financial programs that could provide additional resources needed to grow their businesses.

- Business development where GMKA councils can take advantage of business development services (BDS) centers being established in the districts to disseminate and bridge the information gaps in markets, taxation and business development. Such mechanisms could spur more firm development particularly where they are plugged into more global knowledge pipelines and networks.

- Improving on the burdening taxation procedures of firms. whereby Municipals look towards the successes that have enabled firms to be compliant. For instance some large and medium firms claim to have benefited from the online tax system due to time and cost reductions. These online platforms are replacing the old-style assessments for the trading license which allows too much space for bribery and false assessments. The use of online systems has been extended to small firms, but has not garnered much success for reasons of complex interface, lack of information and illiteracy. Conducting regular training clinics on the use of the online systems could help such firms. In addition, packaging information in a manner that can be understood may simplify processes for the firms and increase on their compliance. Finally, involving existing business associations such as UMA, USSIA and PSFU in order to increase attendance and trust of the private sector.

Other interventions are cross cutting and will require the collaboration of both KCCA, Mukono and Wakiso Municipal councils and government Ministries Departments and Agencies (MDAs).

- For instance addressing knowledge and skills gaps which require involvement of schools and vocational institutes whose training must be tailored to meet the technical

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needs of business. The fact that reputable technical schools are located in GMKA offers an opportunity for the city councils to link up with these institutions and create appropriate programs needed for the market. But this demands that council ally with Ministry of Education and Sports, Ministry of Science and Technology (Responsible for designing these education curriculum) and Ministry of Finance (which funds the implementation of the curriculum).

- City councils need to continuously advocate more investments in infrastructure services particularly electricity distribution and reductions in costs of supply. Aside from working with UMEME, councils will need to work with Electricity Regulation Authority (ERA) to ensure constant supply of electricity at affordable prices. Cheaper services will most likely drive up production of firms and attract more into higher levels of value addition. Other investments that are needed include good road networks throughout the city to facilitate easy access to markets of raw products and materials.

- Establishing of industrial parks for small businesses can help alleviate the land problem and garner increased productivity and therefore increased expansion. Within these spaces, rents are cheap and infrastructure such as electricity and transportation are easily established. Achieving this will require city councils to collaborate with MDA's like the Ministry Of Lands and Urban Development that regulates spaces within urban centers, UMEME that distributes electricity and the Ministry Of Water, Natural Resources and Environment.

Endnotes

1 Government of Uganda (GoU). 2015. National Development Plan II
2 Uganda Bureau of Statistics (BoU). 2016. National Population and Housing Census 2014: Main Report',
3 World Bank. 2013. The Growth Challenge: Can Ugandan cities get to work?, Uganda Economic', Update 5th
4 Pang P (2008). The role of SMEs in Asian development-Statement. Asian Development Bank
Head of Delegation, Hog Kong and China at the 41 st Annual Meeting, Madrid, 5-6 May
5 Uganda Bureau of Statistics. 2011. Census of Business Establishments (COBE),
6 Graduate students from LSE Ms. Samra Bousaba, Mr.Yohannes Iddawela, and Mr. Angus Kathage contributed to the study.

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