

EASE AND COST OF DOING BUSINESS IN UGANDA

What the World Bank 'Doing Business' Report does not tell us

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Introduction

Annually, the World Bank releases the Doing Business report for over 185 countries globally based on their performances across 10 indicators. The report ranked Uganda 132nd out of 185 countries for ease of doing business. Uganda scored poorly in the categories of starting a business and getting electricity, but fared better in the categories of resolving insolvency (Table 1). Uganda has dropped six positions lower than the 2011 position, reflecting a steady decline in the global investor confidence ranking in the past four years.

Table 1: Ease of Doing Business in Uganda rank (out of 189 economies)

Topics	2013	2014	No of Days	
			Uganda	SSA
Starting a Business	146	151	32	29.7
Dealing with Construction Permits	130	143	146	171.1
Getting Electricity	177	178	132	141
Registering Property	128	126	47	58.9
Getting Credit	40	42		
Protecting Investors	113	115		
Paying Taxes	96	98		
Trading Across Borders	164	164		
Enforcing Contracts	114	117	490	652
Resolving Insolvency	68	79	2.2*	3.1*

*Years

Source: World Bank (2014), Doing Business 2014

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The Ease of Doing Business Index rankings are based on metrics drawn from 10 regulations and other factors impacting on a country's business environment. These include: permitting and registering; ease of getting credit and electricity; the legal framework for enforcing contracts and protecting investors; how much tax a company must pay and how a government regulates cross-border trade. These data points are then distilled down to a single score, allowing World Bank researchers to rank all 185 countries the report covers.

Criticism of the Ease of Doing Business Index

Though establishing an economy's aggregate ranking on the ease of doing business compared to other economies and to the regional average which is useful for policy making, the Ease of Doing Business index has been criticized by its ranking based on a small set of indicators. One of the critics; Wall Street Journal noted that, every year the report comes with a disclaimer that it "does not measure the full range of factors, policies and institutions that affect the quality of the business environment in an economy" and, moreover, that within its small set of indicators "the focus is deliberately narrow." The implications of this fine print are quite material, especially if that "small set" of narrow indicators is used by policymakers to drive reforms, thus skewing priorities (WSJ, 2013⁴).

The Wall Street Journal further notes that since the World Bank happens to also be a lending institution, the message and direction of reforms that its rankings suggest are bound to significantly influence public policies in member countries, especially those that depend, or may depend in the future, on its credits or grants. There is evidence that countries, willingly or as a way to access grants or loans, introduce reforms promoted in the Doing Business report (WSJ, 2013).

It is indisputable that Doing Business has been an important catalyst in driving reforms around the world. However, the report is pushing countries to lower taxes and wages and weaken overall industry regulation, thus potentially endangering the poor⁵.

The conceptual flaw Doing Business suffers from is the illusion that a universal numerical ranking can capture the evolution of variables whose significance for development (and even for businesses themselves) are bound to be quite different country to country. World Bank independent panel⁶ warned that aggregation tends to cloud crucial country-level variations⁷. The success of institutional reforms is strongly conditioned by the indigenous environment where they are implemented, an environment which varies country by country. So it is not thoughtless harmonization but attention to the particular requirements and nuances needed in each country and region which will make reform programs successful.

⁴ A Flawed 'Doing Business' Report, May 15, 2013

⁵(<http://www.ipsnews.net/2013/06/world-bank-formally-urged-to-overhaul-doing-business-report>)

⁶ In October 2012, the President of the World Bank Group appointed an independent panel of experts ("the Panel") to review a broad range of issues surrounding the *Doing Business* report

⁷ Independent Panel Review of the Doing Business report, 24 June 2013 Washington, D.C

“...it is important that the Doing Business indicators are not used inappropriately to guide regulatory reforms, as they do not provide the necessary complexity of information, the full picture of what reforms are needed or the different implications of choices that should guide such decisions.”
(Independent Panel Review of the Doing Business report, 24 June 2013 Washington, D.C)

Doing Business in Uganda

In almost all economies, small businesses are vital for sustained growth. A high failure rate is a huge negative for an economy, especially developing economies like Uganda with limited capital. Small businesses are generally regarded as the driving force of economic growth, job creation, and poverty reduction in developing countries. They have been the means through which accelerated economic growth and rapid industrialization have been achieved (Okpara, John O and Wynn, Pamela, 2007⁸).

Uganda’s Private Sector is fragile, largely informal and dominated by Micro, Small and Medium Scale Enterprises (MSMEs). The MSME sector accounts for approximately 90% of the entire private sector, over 80% of manufactured output and contributes about 75% to the gross domestic product (GDP) (MoFPED, 2011⁹). Furthermore, the sector employs more than 2.5 million people, of the total non-farm labour force; with retail trade, education and restaurants accounting for bulk total employment in new firms. However, with exception of education, the rapid growth in enterprises is focused on low-value services (Republic of Uganda, 2010¹⁰).

A study by Uganda Bureau of Statistics (UBOS) in 2011¹¹, found that most of the businesses are located in the Central region (59.2%). The rest are distributed across the other regions as follows: Western (18.0%), Eastern (14.6), and Northern (8.2%). Agriculture, trade, construction and manufacturing are the most important contributors to Uganda’s economy. Figure 1 below shows GDP share by economic activity.

⁸ Determinants of small business growth constraints in a sub-Saharan African economy

⁹ The National Micro, Small And Medium Enterprise Policy (*draft*)

¹⁰ National Development Plan (2010/11- 2014/15)

¹¹ Census of Business Establishments, 2010/11

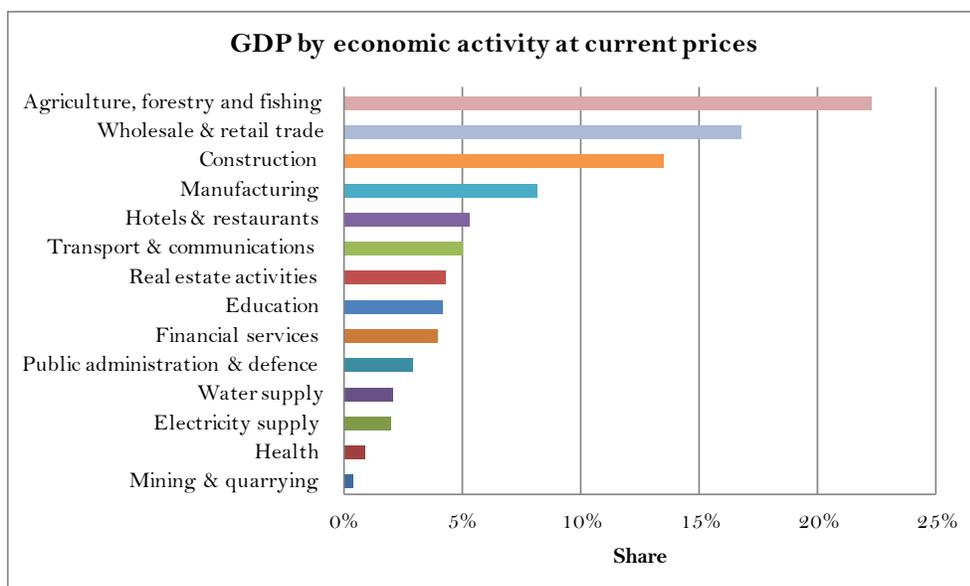


Figure 1: GDP by economic activity in Uganda; Source: Author's based on UBOS Statistical Abstract 2013

While the contributions of small businesses to development are generally acknowledged, entrepreneurs face many obstacles that limit their long-term survival and development. Scholars have indicated that starting a business is a risky venture and warn that the chances of small-business owners making it past the five-year mark are very slim.

Despite the efforts by government to reduce the cost of doing business in Uganda, Small and Medium Entrepreneurs complain of the high cost of doing business in Uganda, which they claim continues to rise and in the process affecting profit margins and causing one of the highest mortality rate of business start-ups in the world. Majority of Uganda's businesses (35%) are aged between 1 and 5 years and those that are 25 years or more are only 4% (PSFU 2013)¹².

Over the past decade, the government has pursued a policy that should provide fertile ground for small business including trade liberalization and making the operating environment more friendly to entrepreneurs. However, the effectiveness of these programs remains unclear, and the rate of business failure continues to increase.

Ugandan entrepreneurs face very high business failure rates, with the majority of businesses failing to make it through their first year of operation. This is partly because many people in Uganda have attempted to start a career in business without the slightest idea of what it entails. It's estimated that about 80% of Ugandans ended up in business by accident with little or prior preparation partly due to high unemployment levels, copy and apply syndrome, and unplanned retirement or retrenchment. Although some easily learn on the job, others spend a lifetime in business without learning even the basics of business management or learn too slow to cope with the ever-changing business environment (Bugaari, 2009¹³).

¹²Private Sector Foundation –Uganda (2013) Platform

¹³ Why most businesses in Uganda die in infancy

Many Ugandans are at first not aware of the extent of their entrepreneurial ability and they don't carry out a market survey to determine the viability of the venture. They start businesses to just exploit what initially looks like a potentially profitable business opportunity only to realize later that they do not have what it takes to become an entrepreneur.

During various engagements and strategic dialogues organized by Agency for Transformation (AFT) with support from USAID / Governance Accountability Performance and Participation (GAPP) with farmers and the business fraternity in Mityana and Mubende Districts (see Figure 2), various participants gave a different account of the bottlenecks encountered in the day to day management of their businesses which included:

- **Centralization of the Uganda Registration Services Bureau services (URSB).** The participants argued that this makes the business registration process for the up-country citizenry longer and the attendant costs of transport and accommodation in Kampala makes the process even more costly. According to a survey conducted by Uganda Small Scale Industries Association (USSIA) among small scale manufacturing businesses in Uganda, only 11% are registered with URSB. The rest are content to operate with licenses obtained at the municipal/town council. Participants also made an observation that at URSB offices, there was a lot of bureaucracy which derails service delivery. This in turn has created middlemen in form of commission agents who charge extra fees to expedite the registration process making the entire process expensive. Indeed, this claim from participants is reinforced by the World Bank's Doing business 2014 report stating that starting a business in Uganda requires an average of 15 procedures and costs an average of 32% of income per capita.
- **Taxation regime that is not clearly understood by most Small and Medium Enterprises (SMEs).** The use of online tax registration and return by Uganda Revenue Authority (URA) is a bottleneck because most SMEs are either computer illiterate or lack access to internet, making the online tax registration and filing a problematic exercise. As a consequence, URA has designated agents for TIN number acquisition and filing taxes, who charge arbitrary fees. This has introduced extra costs for small businesses that seek to comply with the tax regime. Furthermore, local authorities impose other forms of taxation like ground rates, security fees, and trading licenses which are arbitrarily charged sometimes exorbitantly without any assessment of the ability to pay, yet tax dispute appeals always take long and are frustrating.



Figure 2: The AFT CEO, Rwakakamaba Morrison, guiding the workshop

- **High cost and access to electricity.** Only 14% of the population countrywide have access to electricity, and only 7% of the rural population has access to power. The 250 megawatt Bujagali Hydropower Project temporarily alleviated Uganda's power deficit, but demand is growing at 10% per year, which outstrips supply. Government is constructing Karuma hydropower project that will add another 600 megawatts of power to the grid, when it comes online, possibly in 2018. Government is also constructing a number of micro-hydro projects, and is promoting development of renewable energy in Uganda. However, the cost of power installation is high, the supply is insufficient and load shedding is unpredictable and this grossly affects the cost of production and the profit margins of businesses. A study done by IFC in 2013¹⁴, showed that access to power is considered the biggest constraint by a large percentage of firms in Uganda (64%). According to one USSIA enterprise, a bakery, rampant power outages lead to a loss of between 10-20% of the cost of production, as a result of material wastage. However, it's also evident that some SMEs do not know best to cut on electricity costs, such as switching off appliances not in use or controlling machine usage during off-peak hours when the rates are subsidized.
- **High cost of transport.** Transport accounts for up-to 45% of total cost of doing business in Uganda. This is largely due to poor road network especially feeder roads. Efforts have been done in the recent years by government to improve on the road network in Uganda; however, the majority of the funds have been spent on national roads, and less on District, Urban and Community Access Roads (DUCAR), making most DUCAR in bad state.
- **Lack of affordable financing is another impediment for SMEs.** Access to credit is a very big challenge in Uganda. First, these businesses are started with limited capital. Secondly, SMEs lack collaterals such as cars or land titles that can be deposited to get loans from the traditional commercial banks; according to Bank of Uganda¹⁵, only 8% of Ugandans

¹⁴ IFC Jobs Study: Assessing Private Sector Contributions To Job Creation And Poverty Reduction

¹⁵ Status of Financial Inclusion in Uganda

accessed credit from banks in 2013. Loans are generally short term, with interest rates at about 20% or higher and little liquidity exists for longer-term loans. In fact some USSIA and Uganda National Chamber of Commerce and Industry (UNCCI) members complained of being harassed by Microfinance Institutions that use household items as collateral, give relatively small amounts of money, over a short period of time and charge interest that is exorbitant.

- **Corruption and inefficient government services.** Other barriers to doing business in Uganda include high levels of corruption and inefficient government services.
 - **Corruption is part and parcel of most Ugandans;** According to Transparency International's (TI) Corruption Perceptions Index 2013, with score of 26, Uganda ranks 140th out of 177 countries, a worse performance than the 2012's score of 29. TI's 2013 East African Bribery Index ranked Uganda as the most corrupt country in East Africa. Although the blame is always directed at bureaucracy, Ugandan businesses also tend to prefer cutting corners, especially to quickly navigate what they perceive as slow and non-responsive bureaucracy. SMEs in Mityana and Mubende told Agency for Transformation that they would rather bribe a registration officer and quickly get permit instead of spending days in Kampala city where they face expenditures on accommodation and food and lose time.
 - **Inefficient government services.** The attitudes of the most civil servants especially at local government levels is not business oriented and most cases frustrate most business people through unnecessary bureaucracy and 'no care attitude'. At local government level, commercial officers are not fully functional and can't provide any business guidance and information to SMEs.

Enabling environment for SMEs

In many parts of the world in recent years, *Doing Business* data show that there has been remarkable progress in removing some of the biggest bureaucratic obstacles to private sector activity. Yet small and medium-size enterprises still are subject to burdensome regulations and vague rules that are unevenly applied and that impose inefficiencies on the enterprise sector (AfT, 2014¹⁶).

While many countries have acknowledged that small enterprises have an important role in their economies, not much effort has been done to facilitate their growth. They have to compete for finance, markets, personnel, and utilities like any other business units (Mutazindwa, 1997), in Uganda, the Government has only paid a lip service. In fact, the Uganda Investment Authority (UIA) which was set up to promote investments in Uganda is not attractive for the small entrepreneurs. The UIA only supports proposals from companies with more than US\$50,000 to invest. Although UIA has now established an SME division and has done away with most investment incentives the issue of land is still a pertinent one, which is the working space for many MSMEs.

¹⁶ Report of the District-Level Dialogue, Kolping Hotel, Mityana 30th June 2014

The development banks in Uganda did not have programmes for small enterprises. It is easier for a large enterprise to get land for industrial development and a license to operate the business than the SMEs (Balunywa and Sejjaaka, 1997).

Doing Business is not about eliminating the role of the state from private sector development. On the contrary, *Doing Business* recognizes that the state has a fundamental role in private sector development. A key premise of *Doing Business* is that economic activity requires good rules. These include rules that establish and clarify property rights, reduce the cost of resolving disputes, increase the predictability of economic interactions and provide contractual partners with core protections against abuse. The objective is to have regulations designed to be efficient, accessible to all who use them and simple in their implementation (AfT, 2014).

The economies performing best in the *Doing Business* rankings therefore are not those with no regulation but those whose governments have managed to create rules that facilitate interactions in the marketplace without needlessly hindering the development of the private sector (AfT, 2014).

Without good rules that are evenly enforced, entrepreneurs have a harder time starting and growing the small and medium- size firms that are the engines of growth and job creation for most economies around the world.

Recommendations

- Government needs to give fiscal incentives such as tax holidays and tariff concessions to SMEs as well. In terms of monetary support, Bank of Uganda needs to introduce credit guidelines requiring commercial and merchant banks to allocate a portion of their loanable funds to small businesses. Other small business incentive programs should include personnel training, repair and maintenance of specialized machines, and extension services. Small-business assistance programs should also be established by local governments.
- SMEs should not throw business problems/bottlenecks at the government for possible solutions, but rather form coalitions to enjoy the benefits of synergy.
- Entrepreneurs need to find practical solutions to their day-to-day business problems in order to sustain their businesses.
- Uganda's rural private sector players need tremendous technical support in building up capacity and skills in order to keep abreast with latest developments and trends in the business world. The umbrella body (Uganda National Chamber of Commerce and Industry , Uganda Small Scale Industries Association and Private Sector Foundation of Uganda) should endeavor to protect their members by continuously lobbying government to adopt win-win policies, especially in as far as reducing costs of doing business compared to their counterparts in the region in order to make their products more competitive.
- Business people especially SMEs should always follow the budget and planning processes as taxpayers so as to influence policies that are business-friendly.

- Despite the fact that Uganda has initiated a number of regulating bodies with the aim of addressing corruption, it is clear that corruption is societal and done through collusion. There is need for continuous fight against corruption.
- District Chamber of Commerce branches, Farmers Associations, civil society organisations and other business organisations should play an important role in monitoring doing business indicators, voice the concerns of the business community and compelling local government administrations to address problems that increase the cost of doing business.
- Simplify registration processes and procedures using process mapping techniques and consolidated forms that ensure that MSMEs can register themselves quickly and efficiently. Where possible these should be translated in indigenous languages to make them more understandable and acceptable.
- Facilitate district level registrations of MSMEs through the office of the commercial officer liaising with business and farmer organizations.
- Producer companies should be promoted in order to legalise the operations of many MSMEs at minimal cost. These companies have the unique advantage of being a hybrid of a cooperative and a limited liability company.
- Government should roll out e-government services to ensure greater outreach by government departments to MSMEs in rural areas.
- There should be regular district level periodic reviews of regulations affecting MSMEs. This can be done by a joint public-private sector taskforce at districts.

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