Enhancing Green Finance Access for Green Growth

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SEED Practitioner Labs for Policy Prototyping

SEED promoting entrepreneurship for sustainable development

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About the Practitioner Labs for Policy Prototyping

To engage on these opportunities to improve access to Green Finance in Uganda, SEED and ACODE are hosting a Practitioner Labs for Policy Prototyping with the National Planning Authority as the focal point to frame the challenges to be addressed during the labs. With the new Green Finance Strategy available to the public, in particular providers and beneficiaries of Green Finance, ACODE and SEED will co-facilitate group sessions for solutions development and refinement, and support partnership-building efforts. By bringing together different perspectives and experiences, the Practitioner Labs for Policy Prototyping provides an opportunity to build partnerships and develop holistic solutions.

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LIST OF ABBREVIATIONS

AfDB	African Development Bank
APLMA	Asia Pacific Loan Market Association
EADB	East African Development Bank
FAO	Food and Agriculture Organisation
GCF	Green Climate Fund
GDP	Gross Domestic Product
GEF	Global Environment Facility
GGPER	Green Growth Public Expenditure Review
GHG	Greenhouse Gas
IUCN	International Union for Conservation of Nature
LGE	Local Green Enterprises
LMA	Loan Market Association
LSTA	Loan Syndication and Trading Association
MFI	Microfinance Institutions
MSME	Micro, Small and Medium Enterprises
NDC	Nationally Determined Contributions
NDP	National Development Plan
NFIS	National Financial Inclusion Strategy
ODA	Overseas Development Assistance
OECD	Organisation for Economic Co-operation and Development
PSF	Private Sector Facility
SACCO	Savings and Credit Cooperative Organizations
SDGs	Sustainable Development Goals
UGGDS	Uganda Green Growth Development Strategy
UNDP	United Nations Development Programme
UNFCCC	United Nations Framework Convention on Climate Change

INTRODUCTION: GREEN FINANCE

Green Finance is broadly referred to financial investment or activity that has been created to ensure a better environment outcome.[1] Green Finance includes climate finance but is not limited to it and targets financial products and services that consider environmental factors in the lending and decision-making processes to promote responsible investments and stimulate low carbon technologies, industries and businesses. Green Financing plays an important role in delivering Sustainable Development Goals. In the drive to achieve net zero emissions, there is need to re-engineer a range of fiscal, monetary and regulatory policy actions and national and local levels. It is important that to ensure a green transition to a carbon neutral economy particular emphasis should be placed on affordable Green Finance for small and medium enterprises to access financing from banks and other financial institutions.

In the recent years, new methods of financing green projects have been developed including green bonds and green banks. Green banks and bonds have the potential to support clean energy development.[2] Therefore, countries like Uganda must organize their regulatory frameworks to ensure that green borrowing and lending can assist the public sector to develop in a more environmentally friendly direction.

OVERVIEW OF THE STATE OF GREEN FINANCE IN UGANDA

Finance plays a formidable catalytic role in the transition to a green economy. Uganda faces several key challenges on securing financing for the private sector in general and particularly in the green sector. Yet an effective transition to a green economy is dependent on the availability of adequate funding for green initiatives. It is noteworthy that whilst green growth offers immense social, economic and environmental benefits in the long term, it requires huge capital requirements in the long term. Uganda has made significant strides in ensuring Green Finance for the effective transition to a green economy. This section provides an overview of the state of Green Finance in Uganda.

The Uganda Vision 2040 provides development paths and strategies to operationalize Uganda's Vision statement which is '*A Transformed Ugandan Society from a Peasant to a Modern and Prosperous Country within 30 years.*' Accordingly, the concept of the green economy is provided for in Vision 2040. It provides that the green economy will contribute to the eradication of poverty as well as sustaining economic growth, enhancing social inclusion, improving human welfare and creating opportunities for employment and decent work for all, while maintaining the healthy functioning of the ecosystems.[3]

The Uganda Green Growth Development Strategy (UGGDS) 2017/18 – 2030/31 was developed in order to operationalize the green growth broader principles and accelerate the implementation of global development goals, Agenda 2030, Uganda Vision 2040 and the second National Development Plan (NDP II). The UGGDS and roadmap identify finance as an enabling factor that will drive the transition. The UGGDS highlights of some of the major existing financing mechanisms and instruments currently employed for implementing the green economy in Uganda.[4] These include: environmental taxes and levies; compliance charges; local government fees; resource

1 World Economic Forum; What is green finance and why is it important? Nov9, 2020
2 Jeffrey Sachs, Wing Thye Woo & Others ADBI Working Paper Series 2019; Why is green finance important?
3 Uganda Vision 2020 p. 62
4 UGGDS p.26

rents; biodiversity, water resources and climate finance instruments; international funds; non-tax revenue; revenue and benefit sharing and resource access; conservation funds; energy standards and voluntary compliance for trade; subsidies; central government transfers; overseas development assistance (ODA); and private sector contributions.

Nevertheless, the UGGDS observes that most of these revenue streams have been declining to the point where they are unable to provide significant contributions to financing of the green economy targets set.[5] The Strategy therefore proposes six major sources for financing the UGGDS. They include: mobilization from public sector allocations; environmental fiscal reforms and subsidy reforms; sustainable procurement; certification of sustainable production and trade and inclusive green social enterprises; green energy investments and incentives; green innovation and payments for ecosystem services; and international funding.

A Green Growth Public Expenditure Review (GGPER) was undertaken in 2020 and revealed a green growth finance deficit that solidified the need to develop a fully-fledged green financing strategy. The GGPER noted that the green economy transition was slow and inadequate to deliver a green economy and SDGs by 2030. It further indicated that green financing is largely piecemeal, projectized, and ad hoc to deliver the required impact and scale. Additionally, the challenge of duplication of efforts further diluted the transformative of the already meagre financial resources earmarked for implementation of the UGGDS. In the face of these challenges, the GGPER recommended the development of a Green Finance strategy to address with the challenges and enumerate strategies on Green Finance mobilization, utilization, and management.[6] This recommendation in addition to other factors led to the development of the Green Financing Strategy. This Financing Strategy will among others target existing green growth financing windows under climate change and the various environment funds at global and regional levels.

Implementation of the UGGDS is estimated to cost USD 11 billion over its period. This amount has been broken down into cycles corresponding with the national development planning frameworks: USD 2,609 over the short-term period covering 2017/18 -2019/20 - the final three years of the second national Development Plan (NDP II FY2015/16- 2019/20); USD 4,972 over the medium term covering the five years of the NDP III (FY2020/21- FY2024/25), and USD 3,443 over the long term NDP IV (FY2025/26 -2029/30).[7]

According to the Green Finance Strategy[8] public financing for green growth programs is mainly through the National budget, funded through the on-budget and off-budget funding mechanism. According to the GGPER, green growth financing is more inclined to External and GOU financing sources. With green growth projects being heavily financed by external sources, this poses sustainability of financing concerns. Other innovative financing modalities notably, the private sector sources and AIA/non-tax revenue have not been adequately explored.[9] The transition to a green economy requires innovative financing mechanisms such as green bonds and provision of incentives to leverage private sector financing. However, most of these innovative financial mechanisms are yet to be introduced in Uganda and where they exist, they are not efficiently applied.[10]

5 UGGDS P.26
6 Uganda Green Growth Public Expenditure Review Report (UGGPER) p.20
7 Draft Uganda Green Financing Strategy 2021-2030
8 Draft Green Financing Strategy pp.25-26
9 Uganda Green Growth Public Expenditure Review Report (UGGPER) pp.70-71
10 Uganda Green Growth Public Expenditure Review Report (GGPER) 2020 p.17

Table 1: Global and National Legal and Policy context of Green Financing in Uganda: Existing Green Financing Windows

Legal and Regulatory Framework	Green Financing Aspects
Agenda 2030 - SDGs	The 2030 Agenda, particularly SDG 17 on Means of Implementation and revitalized global partnerships highlights the essence of finance in implementing sustainable development initiatives. It emphasizes the catalytic role of Official Development Assistance in complementing domestic resources to actualize a green economy – which is regarded as a vehicle to sustainable development.
Paris agreement, 2015	Under this Agreement, developed countries reaffirmed the commitment to mobilize $100 billion a year in climate finance by 2020, and agreed to continue mobilizing finance at this level until 2025. The money is for supporting climate change mitigation and adaptation in developing countries. It includes finance for the Green Climate Fund (GCF), which is a part of the UNFCCC, but also for a variety of other public and private pledges. The Paris Agreement states that a new commitment of at least $100 billion per year has to be agreed before 2025.
Green Climate Fund	The Green Climate Fund (GCF) was established after COP16 in 2010, with an initial pledge of USD 100 billion per year by year 2020, however, current pledges account for 10million USD. The fund supports both mitigation and adaptation measures in developing countries and keeps operation focus on recipient countries. In order to boost private investments, it set up a private sector facility (PSF) which encourages private participation especially from local SMEs and financial institutions; and enables the poorest nations to participate in the fund.
The Adaptation Fund	Established to finance concrete adaptation projects and programmes in developing countries that are Parties to the Kyoto Protocol. In the first commitment period, the Fund was financed mainly with a share of proceeds from Clean Development Mechanism project activities. For Uganda the accredited Entity to GCF and AF is the Ministry of Water and Environment whereas the Ministry of Finance Planning and economic development serves as the National Designated Authority.

Legal and Regulatory Framework	Green Financing Aspects
Green Loans Principles, 2021	Countries are currently dealing in the aspect of Green Loans and as such, the Loan Market Association (LMA), the Asia Pacific Loan Market Association (APLMA) and the Loan Syndication and Trading Association (the LSTA) developed green loan principles and sustainability linked loan principles to promote transparency in project selection, fund allocation and reporting. The Green Loan Principles of 2021 specify how loan proceeds should be used and how projects should be selected in order to qualify for green-loan status and sustainability loan status respectively. The principles further give categories of eligibility for green loans/projects. The proceeds of a green loan should be credited to a dedicated account so as to maintain transparency and promote the integrity of the product. Developing countries currently account for just $1.6 billion of the estimated $33 billion in outstanding green loans.[11]
Multilateral/Financial Institutions	• The East African Development Bank (EADB) has climate change as one of its focus areas and the bank supports programmes, policies, projects, and technologies towards a low-carbon economy • The World Bank serves as the delivery partner of the Global Environment Facility (GEF) through development Agencies like IUCN, UNDP, and FAO and among others. The Fund gives recipient countries access to funding through accredited national and sub-national implementing entities (including NGOs, government ministries, national development banks, and other domestic or regional organizations that can meet the Fund's standards). • The African Development Bank (AfDB) is active in Uganda in both the energy and agriculture sectors. In the energy sector, the Bank has supported a number of hydropower and other forms of clean energy. • The AfDB Green Bond program facilitates the achievement of the Bank's corporate priority of green growth through the financing of eligible climate change projects. Investors can make a difference with their investment by financing climate change solutions through AfDB's Green Bonds. • UNDP is supporting Uganda in NDCs implementation. • The United Nations Capital Development Fund (UNCDF) is very active in Uganda, engaging both public institutions and small and medium-sized enterprises (SMEs) in the agriculture, energy, education, and healthcare sectors • Standard Chartered has a Green and Sustainable Product Framework that has a theme on Green financing instruments and theme on Access to finance for Financing Microfinance Institutions (MFIs) via intermediaries, and financing of smaller businesses in least developed, low income and lower middle-income OECD DAC markets in which Standard Chartered operates.

11 https://www.worldbank.org/en/news/feature/2021/10/04/what-you-need-to-know-about-green-loans Accessed on 11/08/2022

Legal and Regulatory Framework	Green Financing Aspects
Uganda Revised NDC 2021-2025	In 2018, the government launched Africa's first NDC Partnership Plan, which sets near-term goals that support Vision 2040, the UGGDS and related national strategies. Since 2018, 21 NDC Partnership members have committed USD24 million to turn the Partnership Plan into action. Support includes technical assistance for climate policy, budgeting, training, and action, and financing for flagship projects in key sectors and vulnerable regions. It is estimated that at least US$16.2 billion is required in the form of climate finance to implement the adaptation and mitigation actions prioritized in this NDC, and a combination of public and private finance sources will be utilized to mobilize these funds.
Third National Development Plan 2020/21 – 2024/25 (NDP III)	Dedicates a full programme to Climate change, Environment and Natural Resources in a bid to implement the UGGDS. NDPIII further lists funding Initiatives which are key to national development as some of the innovative mechanisms that would be useful for the GG programs such as concessional loans from multilateral creditors
Uganda Green Growth Strategy (2017/18 – 2029/30)	Proposes six major sources for financing the UGGDS. They include: mobilization from public sector allocations; environmental fiscal reforms and subsidy reforms; sustainable procurement; certification of sustainable production and trade and inclusive green social enterprises; green energy investments and incentives; green innovation and payments for ecosystem services; and international funding.
Uganda Green Finance Strategy	Enumerates strategies on Green Finance mobilization, utilization, and management
Public Finance and Management Act, 2015	Sets out the environment taxes on items like old cars, machines as a way of minimising pollution
Public-Private Partnerships Act, 2015	Provides for the different partnerships agreements a public and private sector can agree on.

MSMEs IN THE UGANDAN ECONOMY

Micro, Small and Medium Enterprises (MSMEs) are often referred to as the engine of economic growth, and identified as key actors who drive innovation, provide job opportunities, generate wealth, and champion socio-economic development, as indicative through the focus given to MSMEs in various NDPs. MSMEs in Uganda provide employment to over 2.5 million people and account for 93.5% of the entire private sector[12], generating over 80% of manufactured outputs that contribute to 20% of gross domestic product (GDP).[13] A number of MSMEs in Uganda operate in the informal sectors. According to the National Small Business Survey, one in five MSMEs in Uganda are not registered, and out of those not registered 51% operate without licenses.

Profile of MSMEs in Uganda

The Uganda Bureau of Statistics provides the following definition for MSMEs in Uganda:

Table: Definition of MSMEs in Uganda, Uganda Bureau of Statistics

	Number of Employees	Total Asset Value	Annual Sales Turnover
Micro	< 5 persons	< UGX 10 million (EUR 2,500)	< UGX 10 million (EUR 2,500)
Small	5 – 49 persons	UGX 10 – 100 million (EUR 2,500 – 25,000)	UGX 10 – 100 million (EUR 2,500 – 25,000)
Medium	50 – 100 persons	UGX 10 – 100 million (EUR 2,500 – 25,000)	UGX 100 – 360 million (EUR 25,000 – 90,000)

Uganda enjoys a strong and stable macroeconomic environment with established support institutions creating an enabling environment for entrepreneurship[14], namely the Directorate of MSMEs under the Ministry of Trade, Industry and Cooperatives (MTIC), Investment and Private Sector Development department under the Ministry of Finance, Planning and Economic Development, and the Uganda Investment Authority. There are also over 35 public and private universities offering business and vocational education and entrepreneurship training.[15] Additionally, other private organisations and intermediaries such as Private Sector Foundation Uganda (PSFU), Enterprise Uganda (EUG), Startup Uganda and many more offer several capacity building and investment opportunities to emerging and growing enterprises. According to the MSME Policy, one in every three Ugandans is engaged in entrepreneurial activity.[16] Globally, Uganda also ranks in the top 3 countries with the most female entrepreneurs, suggesting a robust and dynamic entrepreneur culture that is also gender inclusive.[17]

12 Uganda NDP III (2020-21 – 2024-25), no. 244.
13 Uganda Micro, Small And Medium Enterprise (MSME) Policy (2015).
14 ACODE (2021) „A contextual financial analysis of green micro, small and medium enterprises/local green enterprises in Uganda" Policy Research Paper Series No.105, 2021
15 Uganda Micro, Small And Medium Enterprise (MSME) Policy (2015)
16 Uganda Micro, Small And Medium Enterprise (MSME) Policy (2015)
17 Business Insider, "Uganda, Botswana and Ghana are the world's top 3 economies with the most female entrepreneurs" (18 July 2022) https://africa.businessinsider.com/local/lifestyle/uganda-botswana-and-ghana-are-the-worlds-top-3-economies-with-the-most-female/0kfjp0j

GREEN MSMEs / LOCAL GREEN ENTERPRISES (LGEs) AS DRIVERS OF SUSTAINABLE DEVELOPMENT

Green MSMEs or local green enterprises (LGEs) are enterprises with socially-inclusive and environmentally-friendly business models. They have demonstrated positive contributions to not only economic progress but also positive impacts on the environment and society, proving that economic progress and socio-environmental efforts can (and must) co-exist. Through their business activities and products offered, they help the community save natural resources, reduce carbon footprint, and encourage sustainable consumption and production practices. Socially, they provide quality green jobs (offering living wage, career-building opportunities, fair work environments), particularly also to marginalised groups and drive gender inclusion in the labour market.[18]

Their role is particularly salient in green recovery as a response to the Covid-19 pandemic, as they provide basic products, food, and services to communities that do not always receive support from macro level initiatives. In addition to being green job creators and basic service providers, they also offer green technology solutions, conservation of national ecosystems and resilience building[19] that contribute to green recovery goals.

The nature of green MSMEs / LGEs position them as strategic forerunners in advancing the SDG goals, directly contributing to the country's NDCs. Uganda's NDC seeks to reduce the country's vulnerability to climate change and contribute to greenhouse gas emissions reductions. With limited public finances available for climate change mitigation the private sector is credited for their active involvement in climate action, facilitating technology development and transfer, enabling infrastructure development and providing much-needed finance for climate mitigation efforts.[20] This signals the need to further support and enable the green MSMEs / LGEs who are small scale businesses.

What is an eco-inclusive enterprise

The term "eco-inclusive enterprise" refers to enterprises with business models that are at the core 1) ecological i.e. contributing to the mitigation of and/or adaptation to climate change, or implementing broader environmental and social sustainability measures such as using sustainable production methods, contributing to the efficient use of resources, managing waste, or conserving biodiversity; and 2) inclusive i.e. creating local jobs, in particular for often marginalised populations such as youth, women and low-income households, and through integrating these communities into local and global value chains as suppliers, distributors or customers. Eco-inclusive enterprises are major contributors to poverty reduction and inclusive growth, supporting the achievement of the SDGs.

18 SEED (2022) "Impact Insights: SEED 20 Year Flagship Impact Report."
19 SEED (2021) "Eco-inclusive Enterprises Driving Green Recovery Pathways. A Green Recovery Snapshot"
20 UNDP (2019) „The Business Case For The Private Sector Engagement In Climate Action: Background Report Uganda"

ECO-INCLUSIVE ENTERPRISE SPOTLIGHT

TUSAFISHE

Water, Sanitation & Health (WASH)

Tusafishe produces advertises, sells, and installs automated low-cost filters that eliminate the use of solid fuels to provide safe drinking water for large communities. Together with Finance Trust Bank, customers such as schools have access to flexible loans to acquire the filters. Tusafishe also supplies water filters to non-profit organisations involved in WASH activities, providing installation services and training for the beneficiaries.

Social Impact	Environmental Impact	Economic Impact
• Providing safe water to over 50,000 students in 50 schools. • Reducing water borne diseases amongst students and improving school attendance.	• Reducing dependency on high-carbon water filtering systems. • Reducing up to 10 tonnes of carbon emissions per school.	• Saving each family $465 per annum from medical bills to treat water borne diseases. • Saving schools approximately $14,400 every year from purchasing potable water.

PEEC ENERGY

Clean Energy

Peec Energy works on a proven model of offering remote monitoring and metering for solar mini-grids and pay- as- you -go solar home systems (SHS). It offers PAYG meters to local mini-grid developers to allow them to sell energy in off-grid locations and to remotely monitor their utility assets and collect bill payments via a central software.

Social Impact	Environmental Impact	Economic Impact
• Providing clean and affordable energy access to 3,800 rural off-grid households. • Providing women and youth solar and biogas training and certification from the Directorate of Industrial training.	• Reducing GHG emissions through solutions that make solar more reliable and affordable. • Installed up to 10,000KW generating solar energy systems.	• Supported 250 youth to open small businesses using renewable energy access; solar like kiosks, hair salons and cold drink shops

Access to Finance a Primary Constraint for Growth

Despite making up the majority of the private sector, MSMEs continue to face barriers that hinder sustainable growth, for example, i) high cost of doing business, ii) limited production and organisational capacity, iii) absence of strong supporting environment, iv) weak enforcement of standards, and v) inadequate strategic and sustainable government investments and partnerships with the private sector.[21]

The National Small Business Survey identifies finance as a primary constraint on MSME growth. The MSME Policy also cites limited access to affordable finance and high cost of obtaining credit as a core challenge faced by MSMEs. Enterprises in the early-growth stage remain underserved by financial institutions and face challenges to grow and expand their business models due to the "missing middle" financing gap. This refers to how early-growth businesses are too big for micro-finance but too small for commercial banks. As a result, these businesses are stuck in the scale of "micro" and struggle to expand business activities.

The challenges faced by green MSMEs / LGEs are not particularly different from those of conventional MSMEs. However, the business models of green MSMEs and LGEs that centre social and environmental impact, make them more susceptible to market challenges typically faced by conventional MSMEs. They are still perceived by financiers as riskier business models to invest in, as they are more likely to adopt and promote innovative (unpopular) technologies, alternative revenue models that centre social and environmental returns, and have longer go-to market frames.

21 Uganda NDP III (2020-21 – 2024-25), no. 216; National Small Business Survey (2015)

EcoPlastile

CHALLENGES TO ACCESSING AND DELIVERING GREEN FINANCE

The financial ecosystem in Uganda has experienced remarkable growth over the last months, both formally and informally they have sprouted including numerous commercial banks, development banks such as the Uganda Development Bank, Microfinance Institutions, Savings and Credit Cooperative Organizations (SACCOs), Non-Life and Micro Insurance, Micro Pensions, Agriculture finance, Equity finance companies, Digital financial services and Agent banking among others. Nevertheless, access to green and affordable finance in Uganda's financial ecosystem has been a challenge for most green MSMEs mostly due to structural and other related limitations including:

A) Challenges of MSMEs to Access Finance

i. **Inadequate access to and use of finance.** Although financial resources are available, they are not accessible to the majority of potential users especially the green MSMEs/LGEs. This is driven by low financial literacy especially in the area of digital finance, limited awareness about existing financial opportunities, unstable cash flows, low productivity, low resilience and high probability of failure.

ii. **Inadequate collateral to secure loans.** Much of the SME financing is provided primarily by banks with loans being backed by credit guarantees or collaterals.[22] The theory of social capital puts emphasis on social networks and reciprocity arising from such networks.[23] In the absence of social networks, MSMEs continue to grapple with scarcity of collateral to secure bank loans. Yet, there is evidence that inadequate collateral continues to cripple the financial needs of these MSMEs.[24] This is not to imply that MSMEs do not secure loans from banks. In fact, financial analysts like Kasekende & Opondo (2003) explain that some MSMEs get loans from financial institutions. However, when banks lend to MSMEs, they tend to charge them a commission for assuming risk and apply tougher screening measures, which drives up costs for MSMEs. In addition to collateral, MSMEs are required to demonstrate that they have sufficient equity to contribute to their businesses, which many of them lack.[25] Evidence from the Uganda Securities Exchange (USE) Brochure (2013) indicates that banks consider lack of collateral as high credit risk because of the transaction costs associated with availing credit to such MSME companies.[26] There are various reasons to explain the lack of collateral by MSMEs. What is clear is that limited social networks impede the ability of MSMEs to secure non-collateral securities.

iii. **Informational opaqueness from MSMEs.** No business enterprise can survive early mortality without communication and effective information management.[27] And there is no best way a business enterprise can propel to greater heights if information management is not channelled through social networks in which social capital is derived.[28] MSMEs have always been susceptible to information asymmetries[29] or information opaqueness.[30] Opaqueness makes it is difficult for banks to ascertain if MSMEs have the capacity to pay or willingness to pay if credit is extended to them. This is exacerbated by lack of established information network such as a credit reference bureau for tracking defaulters[31] and unverifiable history of past credits

22 Park (2006); Securitization for SMEs. Korea Institute of Finance, A paper presented at the ADBI Seminar on "Financial Information Infrastructure and SME Finance" held at ADBI, Tokyo, Japan from 9 to 12 May 2006.
23 Putnam, R., (1995) "Bowling Alone: America's Declining Social Capital" Journal of Democracy 6(1): 65-78.
24 UNEP, 2007: Innovative financing for sustainable small and medium enterprizes in Africa. UNEP finance initiave, Geneva
25 Oketch, 2000; Gender Equity. In A. Mullei and A. Bokea (Eds). Micro and small Enterprises in Kenya: Agenda for improving the Policy Environment.Nairobi: ICEG
26 Kurokawa, Tembo, & Velde, (2008) ; Donor support to private sector development in sub-Saharan Africa. Understanding the Japanese OVOP programme, JICA-ODI Working Paper 290. OOT.
27 Maicibi, 2003; Pertinent issues in employee Management M.P.K. Graphics, Kampala
28 Davidsson, P., & Honig, B., (2003). The role of social and human capital among nascent entrepreneurs. Journal of Business Venturing 18(3), pp. 301-331.
29 Oteh, 2010; Making capital markets work for SMEs in Africa. A paper presented as the key note address of the 2010 Kikonyogo Capital Markets Award on 6th May 2010.
30 Torre, Soledad, Peria & Schmukler, 2010; Bank involvement with SMEs: Beyond relationship lending. World Bank, 1818 H St., NW, Washington, DC
31 Apire, 2003; Uganda's Financial Sector and Capital Markets. In UN report, (2003). Proceedings of the symposium on modalities for financing SMEs in Uganda, United Nations. United Nations conference on trade and development, UNCTAD/ITE/TEB/Misc.8, New York and Geneva.

and lack of adequate historical records of the firm's transaction.[32] As Ruffing (2003) explains, lack of financial information increases the transaction costs of banks, or even worse makes it impossible to evaluate the chances of getting their money back if they lend MSMEs.

iv. **Limited technical and management skills.** Many MSMEs lack good quality human capital which also means limited marketing and financial planning, lack of good business plans; poor business records and deficient corporate governance.[33] In addition, due to their small size, a simple management mistake is likely to lead to collapse of MSMEs hence no opportunity to learn from its past mistakes.[34]

v. **Lack of professionalism.** There is evidence to the effect that MSMEs in Uganda lack professionalism.[35] This is exhibited in corrupt tendencies[36] disrespecting business contracts[37] and deliberate concealing of business records on transactions.[38] Other ethical issues include unfair treatment of stakeholders and manipulation of organizational structure.[39] There are also concerns of lack of professionalism outside the control of MSMEs such as dubious legal systems.[40] These ethical concerns have discouraged banks from lending to SMEs. In the absence of ethical environment and trust, SMEs lose out on capital financing as well as deprivation of social capital advocated for by the theory of social capital. These are further exacerbated by a general weak enforcement of standards due to weak monitoring and supervision systems.

vi. **Competition from large enterprises.** MSMEs always face competition in accessing finance and markets.[41] A number of survey-level studies have found that MSMEs face greater obstacles than large firms both in terms of accessing finance and the underlying cost of credit.[42] Yet, limited accessibility to markets constrains MSMEs from generating capital needed to run daily business operations. Compared to large enterprises, MSMEs are less efficient and incur high costs per unit of revenue.[43] They use labour-intensive technologies compared to larger firms making them miss out in benefiting from economies of scale. Besides, Ugandan MSMEs face competition from the global economy too.[44] With poor technology, competition for markets and inadequate finance, MSMEs cannot expand to serve global markets or even establish business linkages with larger firms. Moreover, they cannot acquire credit ratings that satisfy investors.[45] MSMEs are typically required to demonstrate that they have sufficient equity to contribute to their businesses, which many small business owners usually lack.[46] However, larger, older, and foreign firms have a much easier time accessing expansion and development capital than MSMEs.[47] Consequently, many MSMEs stay small and informal and use simple technology.[48] The non-symbiotic relationship between large firms and MSMEs due to competition implies that the duo may not develop social networks from which to derive social capital. This continues to affect the ability of MSMEs to access finance.

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32 *Oteh, A., (2010). Making capital markets work for SMEs in Africa. A paper presented as the key note address of the 2010 Kikonyogo Capital Markets Award on 6th May 2010.*
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46 *Kasekende, L., & Opondo, H., (2003). Financing Small and Medium-Scale Enterprises (SMEs): Uganda's Experience, Bank of Uganda Working Paper.*
47 *Leo. B., (2011). "New SME Financial Access Initiatives: Private Foundations' Path to Donor Partnerships."CGD Working Paper 254. Washington, D.C.: Center for Global Development.*
48 *Kauffmann, C., (2005). Financing SMEs in Africa, Policy insight No.7, EOCD Development Centre.*

B) Challenges of Finance Institutions in Providing Finance to MSMEs

i. **Underdeveloped financial segments and products.** The capital and financial markets in Uganda are still relatively weak. Innovative financial products especially those based on Digital Financial Services are relatively few and inaccessible to potential customers especially those in the rural and informal sectors. Relatedly, Uganda has only one development bank which is also undercapitalised. Additionally, the use of digital payments for bill payments is still under appreciated. Whilst mobile money has been embraced, usage of other digital platforms such as credit cards and insurance payments are still in its nascent stages partly due to the fact that Uganda is still largely entrenched in a cash economy.

ii. **High cost of finance.** Despite reforms in the private sector, interest rates in Uganda remain high between 20-23%. In addition, to access funds from financial institutions, MSMEs face stringent financial requirements, such as having sufficient collateral. This situation is reflected in the negligible proportion of MSMEs (0.4%) who actually borrow from micro-finance institutions.[49]

iii. **Availability of long-term finance is very limited.** The capital markets infrastructure is still underdeveloped while the innovation and supporting infrastructure is also weak. Although, there are many relevant policies and regulatory frameworks, there are still many outstanding implementation challenges.

iv. **Unfamiliarity with green business models.** Financial institutions and investors are still mostly unfamiliar with green and socially inclusive business models and growth trajectories, which involve what are perceived as riskier technologies and longer go-to market time frames. Investors and financial institutions do not readily offer tailored financial solutions[50] that for example align lending requirements with readily available collateral, repayments based on business seasonality, enable investments in new resource-efficient technologies and more.

49 National Small Business Survey (2015)
50 "International Finance Corporation (2017) "MSME Finance Gap: Assessment of the Shortfalls and Opportunities in Financing Micro, Small, and Medium Enterprises in Emerging Markets". https://openknowledge.worldbank.org/handle/10986/28881

Awamo Water Solutions

OPPORTUNITIES TO ELIMINATE BARRIERS TO ACCESS GREEN FINANCE IN UGANDA

I. **Supporting the National Financial Inclusion Strategy (NFIS) 2017-2022**[51] focused on ensuring that all Ugandans have access to, and use of a broad range of quality and affordable financial services which help to ensure their financial security. The strategy targets to reduce financial exclusion from 15% in 2017 to 5% in 2022.[52] The NFIS has five pillars namely: Reduce financial exclusion and barriers to access financial services; Develop credit infrastructure; Build digital infrastructure; Deepen and broaden formal savings, investment and insurance usage; and Protect and empower individuals with enhanced financial capability. Other crucial action points in the Strategy are highlighted, including: Establish lines of credit to critical sectors such as Housing, MSME, and Agriculture with the aim of growing the credit market; Conduct a review of the tax, regulatory and legal obstacles for all products; Promote utilisation and uptake of the agriculture insurance facility; and Strengthen linkages, knowledge-sharing, and effectiveness of value chains.

II. **Enhancing information management and improving management skills in MSMEs.** One of the critical challenges limiting MSMEs from accessing finance in Uganda is informational asymmetry and lack of competent and motivated workers. There are ways in which MSMEs can neutralise these challenges including relationship lending enhanced by social networks.[53] Through social networks, MSMEs can learn best practices to manage information for effective business transactions, and adopt clear accounting standards. Reliable business information can be enhanced through independent and reputable accounting firms, as well as credit bureaus who can supply data on the solvency of firms. These allow banks to obtain trusted information about the MSMEs from reliable third parties.[54] Making available continuous training of staff to make sure they deliver based on the standards of the institution is another way to uphold business standards.

III. **Providing technical business development support services to MSMEs**/LGEs as a mandatory prerequisite for their access to finance (e.g. when selected to receive a loan from a bank) to ensure effective utilisation of finance, human and materials resources.

IV. **Improving MSMEs' personnel capabilities** through training and upskilling of personnel to adopt digital technologies that enhance a firm's competitiveness and productivity. This training can be promoted to not only enable firms to improve operations but encourage innovation and adaptation to socio-economic and climate change shocks, ultimately to emerge more resilient from such training.

V. **Implementing targeted environment fiscal reforms, subsidies, fiscal tools** such as tax exemptions/reductions on energy, green products, inputs, machinery and equipment produced or used by MSMEs/LGEs in order to make them more competitive, innovative and access green technologies.

VI. **Fast tracking the development of a national green growth financing strategy** to guide the process of mobilising and use of financial resources by MSMEs/LGEs and facilitate the implementation of the UGGDS. For example, the Uganda Green Finance Strategy focuses on increasing Green Finance streams for Uganda, mainstreaming green growth financing, and using these levers towards poverty alleviation and green job creation to ensure a sustainable future.

51 https://www.bou.or.ug/bou/bouwebsite/bouwebsitecontent/publications/special_pubs/2017/National-Financial-Inclusion-Strategy.pdf
52 Republic of Uganda. National Financial Inclusion Strategy 2017-2022
53 Torre, Soledad, Peria &Schmukler, 2010; Bank involvement with SMEs: Beyond relationship lending. World Bank, 1818 H St., NW, Washington, DC.
54 Kauffmann, C., (2005). Financing SMEs in Africa, Policy insight No.7, OECD Development Centre. Kiiru, W. K. (1991). A review of the institutional lending to the Jua Kali and small enterprise sector in Kenya. Geneva: International Labour Organisation

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